SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934

No. 663

JOHN A. SNYDER, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

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JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., FEBRUARY 14, 1935.

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[fol. 1]

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 49721

JOHN A. SNYDER, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appearances: For Taxpayer: Harry A. Fellows, Esq., Henry M. Ward, Esq.
For Comm'r: R. W. Wilson, Esq., W. W. Kerr, Esq.

DOCKET ENTRIES

Aug 4, 1930.	Petition received and filed. Taxpayer notified. (Fee paid.)
Aug. 5, 1930.	Copy of petition served on General Counsel.
Sept. 12, 1930.	Answer filed by General Counsel.
Sept. 1[illegible], 1930.	Copy of answer served on taxpayer. General Calendar.
Mar. 15, 1932.	Hearing set May 5, 1932.
Apr. 26, 1932.	Motion for continuance filed by taxpayer. 4/27/32, granted to Fall 1932.
Sept. 13, 1932.	Hearing set Oct. 27, 1932.
Oct. 15, 1932.	Motion for 90 days continuance filed by taxpayer. 10/19/32, granted to 1/25/33.
[fol. 2] Oct. 15, 1932.	Notice of appearance of Henry M. Ward as counsel filed.
Jan. 18, 1933.	Motion for 60 days continuance filed by taxpayer. 1/19/33, granted to 3/27/33.
Mar. 22, 1933.	Motion for leave to file amended petition, amendment tendered, filed by taxpayer.
Mar. 23, 1933.	Motion for continuance to a date not prior to May 15, 1933, filed by General Counsel.
Mar. 24, 1933.	Copy of motion and amended petition served on General Counsel.
Mar. 27, 1933.	Hearing had before Mr. Marquette on merits. Petitioner moves to amend petition—granted. Leave to amend answer granted. Continued to May 22, 1933.

Mar. 27, 1933. Order that amended petition lodged on March 22, 1933, be filed and respondent be given the usual time to answer and to continue proceedings for hearing on the merits to May 22, 1933, entered.

Apr. 24, 1933. Answer to amended petition filed by General Counsel. 4/28/33, copy served.

May 22, 1933. Hearing had before Mr. Arundell on merits. Submitted. Briefs due 6/30/33.

May 31, 1933. Transcript of hearing of May 22, 1933, filed.

[fol. 3] June 27, 1933. Motion for extension of 30 days from June 30, 1933 to file briefs filed by taxpayer. 6/27/33, granted.

July 29, 1933. Brief filed by taxpayer.

Sept. 14, 1933. Opinion rendered, C. Rogers Arundell, Div. 7. Decision will be entered for the respondent.

Sept. 16, 1933. Decision entered, Eugene Black, Div. 15.

Dec. 1, 1933. Supersedeas bond in the amount of $78,000. Approved and ordered filed.

Dec. 5, 1933. Petition for review by U. S. Circuit Court of Appeals (3) with assignments of error filed by taxpayer.

Dec. 5, 1933. Proof of service filed.

Dec. 13, 1933. Agreed statement of evidence lodged.

Dec. 13, 1933. Agreed statement of evidence approved and ordered filed.

Dec. 20, 1933. Præcipe with proof of service thereon filed by taxpayer.

[fol. 4] BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

AMENDED PETITION—Filed March 27, 1933

The above-named taxpayer hereby petitions for a redetermination of the deficiency determined by the Commissioner of Internal Revenue as set forth in his deficiency

letter dated June 6, 1930 (IT:AR:B-6:JMF-60D) and as a basis for this proceeding sets forth the following:

I. The petitioner is an individual residing and doing business in Philadelphia, Pennsylvania.

II. The said notice of deficiency, a copy of which is attached and marked Exhibit "A," was mailed to the petitioner on June 6, 1930 and within sixty days thereafter and on August 4, 1930 the petitioner filed his petition for redetermination with the Board of Tax Appeals.

III. The taxes in controversy are personal income taxes for the calendar year 1928 in the amount of $38,961.22.

[fol. 5] IV. The petitioner submits that the determination of the Commissioner is erroneous in the following respects:

(a) The Commissioner increased petitioner's taxable income for the year 1928 in the amount of $192,143.25, claimed to represent profits from the sale of stock certificates.

(b) The sole basis for increasing petitioner's taxable income in the amount stated was the application by the Commissioner of Article 58 Regulations 74, which provides as follows:

"When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots can not be determined, the stock sold shall be charged against the earliest purchases of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain. * * * "

(c) The said regulation is inapplicable to the transactions in the purchase and sale of shares of stock by brokers for account of petitioner during the year 1928 as more fully set forth herein.

(d) If applicable to such purchases and sales as herein set forth, petitioner submits that the said Article 58 above quoted was beyond the power of the Commissioner, was not authorized by law, and was in violation of rights secured to petitioner by the Constitution of the United States and particularly by the first clause of the First Section of the First Article, and by the Fifth Amendment, in that in mak-

ing such regulation the Commissioner attempted to exercise legislative power which by the First Section of the First Article of the Constitution is vested in the Congress of the United States and in that application of said article of said regulation deprives petitioner of his property without due process of law in violation of the provisions of the Fifth Amendment of the Constitution.

[fol. 6] V. The facts upon which petitioner relies in support of his petition are as follows:

In the years immediately preceding the calendar year 1928, and particularly in the years 1925, 1926, and 1927 petitioner, in addition to his regular employment as secretary of an insurance company on salary, was engaged in a business regularly carried on for profit, and in certain transactions entered into for profit, which business and transactions were the purchase and sale of shares of stock listed on the New York and Philadelphia Stock Exchange, carried on by the petitioner through stock brokers who were members of said stock exchanges. The said business and transactions had been carried on continuously by petitioner during the said prior years particularly in 1925, 1926 and 1927. During the period prior to 1928 (with one small exception which does not affect the questions involved) petitioner's operations in the stock market were confined to the purchase and sale of shares of the capital stock of only one corporation, namely United Gas Improvement Company, a public utility engaged in business and operating in the City of Philadelphia, Pennsylvania, and elsewhere. The said corporation is herein referred to for brevity as "U. G. I." the name by which it is commonly known in stock exchange transactions. Said corporation had a large share capital and its shares were among the most active and most largely dealt in in said stock exchanges.

VI. During the period prior to and throughout the year 1928 petitioner traded in said U. G. I. stock exclusively through margin accounts with stock brokers, and from time to time during said period increased his holdings of such stock solely through the process known as "pyramiding" as more fully hereinafter described. At the end of the year 1927 the petitioner had two margin accounts [fol. 7] with stock brokers; one with the firm of C. Clothier

Jones & Company, of 1603 Walnut Street, Philadelphia, and the other with MacDonald & Company, 234 Real Estate Trust Building, Philadelphia, Pennsylvania. Both of said accounts were margin accounts and all the shares of stock of U. G. I. bought by each of said brokers had been bought for account of petitioner through the process of "pyramiding" on a rising market. On the first day of January, 1928, said firm of Clothier Jones & Company held for account of petitioner as the result of the prior transactions to and including December 31, 1927, 2300 shares of U. G. I. stock against which there was a debit balance against petitioner on the books of said firm of $218,696.95. On the first day of January, 1928, said firm of MacDonald & Company, held for account of petitioner, as the result of the prior transactions to and including December 31, 1927, 3000 shares of U. G. I. stock against which there was a debit balance against petitioner on the books of said firm of $283,168.64.

VII. During the year 1928, from the 1st of January to the 31st of December, inclusive, the petitioner continued his operations in the stock market in U. G. I. stock through the said two brokers, both of whom were members of the New York and Philadelphia Stock Exchanges and carrying on their business in accordance with the established practice, rules and regulations of said Stock Exchanges. From time to time during the year 1928 the petitioner instructed said firm of Clothier Jones & Company to purchase and carry for his account and risk additional shares of said U. G. I. stock and to sell for his account certain shares of said stock. The total number of shares of said U. G. I. stock so sold by said brokers for account of the petitioner in 1928 was 3700, making an excess of U. G. I. stock purchased and held by said firm of Clothier Jones & Company [fol. 8] for account of the petitioner over the shares sold of 1200 shares, so that the number of U. G. I. shares carried by said brokers for account of the petitioner had increased in 1928 from 2300 to 3500 and the debit balance on the books of said firm of Clothier Jones & Company had increased from $218,696.95 on January 1, 1928, to $407,294.70 on December 31, 1928. The said balances on said dates and the intermediate balances on the first day of each month as reported to the petitioner by said brokers were in accordance with the customary course and practice of

business on the Stock Exchanges of New York and Philadelphia, reached by debiting petitioner with the purchase price of the U. G. I. stock purchased for his account on his orders together with all commissions, taxes, interest, and other debit items and by crediting his account from time to time with all proceeds of sale and with all dividends received by said brokers upon certain of the shares of stock carried by them for account of the petitioner.

VIII. From time to time during the year 1928 the petitioner instructed said firm of MacDonald & Company to purchase for his account and risk additional shares of said U. G. I. stock and to sell for his account certain shares of said stock. The total number of shares so purchased by said firm of MacDonald & Company during the year 1928 on petitioner's orders was 5700 and the total number of shares of U. G. I. stock so sold by said brokers for account of petitioner was 4200, making an excess of U. G. I. shares held by said firm of MacDonald & Company for account of petitioner over the shares sold of 1500 shares, so that the number of U. G. I. shares carried by said brokers for account of the petitioner had increased in 1928 from 3000 to 4500 and the debit balance on the books of said firm of MacDonald & Company had increased from $283,169.64 on [fol. 9] January 1, 1928, to $525,527.97 on December 31, 1928. The said balances on said dates and the intermediate balances on the first day of each month as reported to the petitioner by said brokers were, in accordance with the customary course and practice of business on the Stock Exchanges of New York and Philadelphia, reached by debiting petitioner with the purchase price of the U. G. I. stock purchased for his account on his orders together with all commissions, taxes, interest, and other debit items and by crediting his account from time to time with all proceeds of sale and with all dividends received by said brokers upon certain of the shares of stock carried by them for account of the petitioner.

IX. With respect to the transactions in the purchase and sale of U. G. I. stock through said two brokerage houses petitioner throughout the year 1928 was attempting to and did take advantage of the fluctuations in the market quotations of said U. G. I. stock, with the intent and purpose of increasing the number of shares of U. G. I. stock carried for his account by said brokers. By selling from time

to time in 1928 a part of the additional purchases of said stock petitioner was taking advantage of the turns of the market, selling stock from time to time when the market quotations were higher or slightly lower than at the time of purchase in the year 1928 and buying back equivalent amounts of stock when the quotations were lower or slightly higher, but the market was still rising.

X. During the said period from time to time the said brokers in fulfillment of selling orders given them by petitioner sold more U. G. I. stock than they then had on hand as a result of the purchases made for petitioner's account in 1928, but in each of such instances petitioner had given orders to sell various amounts of such U. G. I. [fol. 10] stock at the quotations in force on the day of sale, with the intent and purpose of buying back equivalent or greater amounts of such stock shortly thereafter, whenever the market quotations were sufficiently low to show a profit or only a small loss on the transaction. This intention was carried out and as above set forth petitioner caused the said brokers to purchase for his account during the year 1928 many more shares than he instructed them to sell for his account. All of such purchases and sales were made by said brokers, under petitioner's instructions, in the carrying out of the said business and transactions entered into by petitioner through the said brokers for the purpose and in fulfillment of the petitioner's increasing his holdings of said U. G. I. stock in the said margin accounts through the said process of "pyramiding" and it was not petitioner's intention at any time to have the said brokers sell for his account any of the shares of stock purchased in prior years or to realize any profit with respect to the earlier purchases. Petitioner's intention in general throughout the year 1928 was to increase the holdings of U. G. I. stock carried for his account by said brokers to as great an extent as the margin of his account permitted. Throughout 1928 said brokers, in accordance with the established practice of stock brokers and their customers in the purchase and sale of stock certificates on margin accounts, required petitioner to maintain at all times a sufficient credit balance or margin. This margin was represented by the difference between the current market quotations of all the shares of U. G. I. held by said brokers for his account and the debit balance against petitioner, rep-

resented by the amount paid for stock purchased and other debit items. Throughout the year 1928, as in prior years, petitioner was required by said brokers to keep at all times a "margin" or credit balance so computed, of not less than [fol. 11] 30 per cent, so that his debit balance might not exceed at any time 70 per cent. of the total credit balance computed on the basis of the daily market quotations of said U. G. I. stock, multiplied by the number of shares carried by the brokers to the credit of petitioner's account. Whenever because of a fall in the market quotations, petitioner's debit balance was in excess of 70 per cent. of his credit balance so computed said brokers required petitioner either to put up more margin in the form of cash or securities or to increase his credit balance by selling a sufficient number of shares of U. G. I. In all such instances petitioner ordered his brokers to sell and they sold accordingly a sufficient number of shares to make good petitioner's margin. In such instances the lack of a sufficient credit balance had been brought about by the debit having been increased through the most recent purchases and through a fall in the market, and in all such cases it was the intention of petitioner in accordance with the usual and established course of trading on the Stock Exchange to sell the stock last acquired, the purchase of which followed by the fall in market quotations had impaired his margin.

XI. The well-established course of dealing on the Stock Exchanges in New York and Philadelphia in the purchase and sale of securities through stock brokers in accordance with which all the transactions herein set forth were carried on is and was in the year 1928, with respect to margin accounts, substantially as follows:

The person desiring to operate in the stock market known as the "customer" gives to the stock broker orders, oral or written, to buy or sell, as the case may be, a designated number of shares of a designated stock. If the transaction is a purchase or a "long" transaction on margin the customer advances or "puts up" with the broker such percentage of the cost of the stock as may be required for [fol. 12] "margin." In 1928 the customer's margin required was usually not less than 30 per cent. and not over 40 per cent. depending on the activity of the stock and the credit rating of the customer. In some cases a cus-

tomer was allowed as was petitioner to some extent to keep a margin of less than 30 per cent. in dealing in certain active stocks such as U. G. I. Where all the transactions, as in the case of the petitioner, are in lots of 100 shares or multiples of 100 shares and there are no "odd lot" transactions, the broker executes the order on the floor of the Stock Exchange by purchasing the number of shares ordered. Under the rules of the Stock Exchange, which are binding upon all stock brokerage houses, members thereof, delivery of the stock must be made to the broker who buys, from the broker who sells, not later than the following day. In all cases where a margin account is involved, that is to say where the stock is not to be bought outright fully paid for and put in the name of the customer on the books of the company, the delivery of the stock is always made in the form of what is known as a "street certificate." A "street certificate" is a certificate for 100 shares of a designated stock listed on the New York or Philadelphia Stock Exchange, standing on the books of the corporation in the name of a brokerage house, a member of either Exchange. This stock certificate, endorsed in blank by the brokerage house in whose name it stands and is delivered not later than the following day to the broker who has purchased it. "Street certificates" in this form pass from hand to hand among the brokerage houses with the same freedom as currency or bank notes and are not customarily put in the name of the broker to whom or of the broker by whom the delivery is made. By agreement between the customer and the broker, as long as the certificates are carried by the broker on margin for [fol. 13] account of the customer, the broker has the right, which is customarily exercised and was exercised by the said brokers through whom the petitioner carried on his operations, of pledging such "street certificates" with banks or trust companies as collateral security for loans. In the course of the brokerage business large brokerage houses such as the said firm of C. Clothier Jones & Company and MacDonald & Company, have thousands of customers and carry for accounts of their various customers on margin many thousands of "street certificates." These "street certificates," together with other securities (such as bonds also carried by brokers for account of their customers who are dealing in bonds) are pledged with banks

and trust companies for loans of amounts which are required to meet the payments from day to day required for the purchase of securities by the brokers for account of their various customers. Banks and trust companies are not permitted to and will not make loans to brokers in excessive amounts, so that the brokers are required to and do make loans from many different banks and trust companies in the aggregate amounts needed. As collateral for these various loans, which the case of such large brokerage houses as those mentioned herein run into many millions of dollars, the brokers mingle all the "street certificates" which they happen to be carrying in one particular stock, such as U. G. I., with other street certificates of other stocks and the identity of the "street certificates" so pledged for the account of any particular customer is completely lost. Consequently it has been at all times since long before the establishment of the regulation of the Commissioner above referred to and continuously thereafter, impossible to identify in any active stock which the broker is carrying for the account of more than a few customers any certificate purchased for the account of any particular customer.

[fol. 14] XII. With respect to sales of stock certificates by brokers, the usual course of procedure, which was followed with respect to petitioner's account and has been followed at all times since long prior to the making of the said regulation and continuously thereafter, is that when the broker is required to make delivery of the certificates sold, he takes whatever "street certificates" of the particular stock may be the most conveniently available, either from such lot of street certificates of the particular stock as the broker may have in his office, or out of street certificates so pledged with some bank or trust company, in that case either paying off part of the loan or substituting other collateral. Consequently, for example, when in the instant case either broker executed an order given him by petitioner for the sale of one hundred, or a multiple of a hundred, shares of the U. G. I. stock, the broker did not necessarily or usually sell any one or more of the particular street certificates purchased for account of the petitioner, but in most instances sold street certificates held for account of other customers.

XIII. Under the custom and usage of the brokerage business, as carried on by brokers, members of the New York or Philadelphia Stock Exchanges, and under the contractual relations existing between all customers of such brokers operating margin accounts (including petitioner and the brokers above specified), the customer did not, nor did the petitioner in any instance, when a purchase was made for his account upon his order, acquire title to any specified certificates. What he acquired when he gave his broker an order to buy stock was the right to demand from the broker at any time delivery of an equal number of shares of the particular stock so purchased, but he did not acquire the right to delivery nor would delivery be made to him by the broker until, with respect to the shares of [fol. 15] stock so to be delivered, he had paid to the broker in cash or securities a sufficient amount to represent the aliquot part of the debit balance on the books of the broker attributable to the shares of stock to be delivered. A customer had not the right to demand delivery of any certificates without such payment if such delivery would result in reducing his credit balance of long stock carried for his account below the amount required for margin as above stated.

XIV. Throughout the year 1928 petitioner did not — any time require either of said brokers to deliver any stock to him nor did the petitioner at any time during the year 1928 make any further payments to either of said brokers either in cash or securities, but petitioner relied solely upon the "paper profit" which would have been realized at any time if the account had been closed and the shares of U. G. I. which the brokers were carrying for his account sold at current quotations and the proceeds of sale less the debit balance had been paid over to him. Throughout the year 1928 as the result of the operations of petitioner as herein above set forth these "paper profits" were sufficient, on a rising market, to enable the petitioner to accumulate during the year in his accounts with the respective brokers the numbers of shares above specified, and all of the transactions in the year 1928 with the said two brokers in the purchase and sale of U. G. I. stock were made for the purpose and had the effect of strengthening petitioner's position in the stock market, increasing his margin of "paper profit" and thereby enabling him to increase his holdings

and occupy the position which is commonly known as being "long" on the stock market.

XV. Under the rules and practice of the said stock exchanges the brokers were required to and did in each in-
[fol. 16] stance of a purchase or sale as the case might be for account of petitioner and for account of any and all other customers, deliver to petitioner, by mail or otherwise, on the day of purchase or sale, a memorandum of such purchase or sale stating the number of shares bought or sold, the name of the stock, and the name of the brokerage house from whom the stock was bought or to whom the stock was sold, as the case might be. The name of the broker from whom the stock was purchased did not necessarily, although it might, represent the broker in whose name the street certificate or certificates bought, stood on the books of the company and by whom the street certificate or certificates were endorsed. Neither of the said brokers at any time throughout the year 1928 caused any of the street certificates bought for account of petitioner to be put in his name on the books of United Gas Improvement Company nor did they customarily do so with respect to the thousands of other customers for whom they were carrying margin accounts. With respect to the U. G. I. stock sold none of the sales was made of any stock standing in the name of the petitioner but all such sales were made of street certificates, either those which happened to be in the office of the broker by whom the sale was made or those which might be taken out of securities pledged with banks or trust companies as above stated.

XVI. In making the purchases for petitioner's account and for account of the thousands of other customers which the said brokers were carrying on margin the transactions with respect to paying for the stock were substantially as follows:

The loans made by the respective banks and trust companies were on the basis of approximately 50 per cent. of the current market quotations of all the securities pledged
[fol. 17] as collateral for the various loans, so that, as market quotations rose the amount of loans could be increased, but as the market quotations fell, the amount of loans had to be curtailed or additional securities pledged. The cash supplied by petitioner to brokers together with the paper

profits as above described represented from 30 to 40 per cent. of the current daily quotations. The balance, namely, from 10 to 20 per cent., was supplied from the broker's working capital. This basis of transacting business was universally adopted with respect to all stocks listed on the New York and Philadelphia Stock Exchanges by all brokerage houses members of either or both of such exchanges. With respect to all margin accounts it had been adopted and was well recognized many years before the said regulation of the Commissioner was put into effect and was continuously in operation thereafter.

XVII. Petitioner submits as a particular ground for attacking the validity of the said regulation of the Commissioner, that it assumes a non-existent fact, namely, that there is any way in which in the case of any active margin account in an active stock such as U. G. I. it is possible to establish the identity of any certificate purchased or sold as the case may be, by a broker for account of his customer. Petitioner submits that the effect of this regulation, as applied to the facts in this case, is to make it impossible for petitioner to prove, as the fact is, that it was not his intention to sell at any time in the year 1928 any of the stock acquired in prior years which showed a large profit, and that it was not his intention at that time to realize any such large profit, but in the course of the transactions above described his intention was, and the effect of his acts was merely to strengthen his position in the market, and by realizing profits on the particular transaction of the year 1928 to increase his margin account and thereby [fol. 18] to enable his brokers to purchase for his account in the manner and on the basis above described, the additional shares of U. G. I. as above stated.

XVIII. Petitioner submits, therefore, that with respect to petitioner's transactions herein set forth the said regulation is wholly arbitrary and has no reasonable basis or justification, but was devised by the Commissioner of Internal Revenue during a rising market with the purpose and intent of increasing the amount of income tax chargeable against petitioner and other taxpayers similarly situated to as great an extent as was practicable, and thereby without warrant of law to penalize them by the imposition of arbitrary and oppressive taxes in connection with their

lawful purchases and sales of stock on margin accounts in accordance with the established practice of the Stock Exchanges of New York and Philadelphia and of other stock exchanges. Petitioner further submits that if the Commissioner has power to make this particular regulation with respect to a rising market, he has equally the power to make the opposite regulation with respect to a falling market and thereby to prevent the petitioner and others similarly dealing in stocks on margin accounts from deducting losses actually suffered by reason of their intent and purpose to sell the stock which show the largest losses.

XIX. It was the intent and purpose of petitioner and of the said brokers through whom he was operating in every instance, either to sell the last acquired stock first or to sell one or more hundred shares of stocks in the form of "street certificates" and shortly thereafter, when the market had fallen, to buy back an equivalent number with the purpose and intent of increasing petitioner's margin and thereby enabling him to have the said brokers acquire for [fol. 19] his account and to go "long" of additional shares of U. G. I. stock with the hope and expectation at such time in the future as the market might further rise, of selling all or a large part of his shares of U. G. I. stock at a great profit. There was no object, and it could not have been of any benefit or advantage to the petitioner to realize and convert into cash the paper profits which represented the great increase in the market quotations of U. G. I. stock from the time of purchase thereof in prior years to the time of the sale thereof in 1928. During the said period the market quotations of said stock were in many cases 100 or more points, that is to say 100 or more dollars per share, over and above the price at which they had been purchased in prior years. Under the course of trading adopted by petitioner no substantial profits could have been realized and drawn by the petitioner from his account with said brokers without impairing his margin and thereby making it impossible for him to accumulate in his account the additional shares of U. G. I. stock.

XX. Attached hereto as a part of this petition and marked Exhibits B and C are summary statements by months of all the transactions in U. G. I. stock herein referred to in the year 1928 in the two margin accounts with

C. Clothier Jones & Co. and MacDonald & Co. respectively showing the number of shares "long" to petitioner's credit on January 1, 1928, and at the end of each month, the number of shares bought and sold with dates of purchase and sale respectively, the debit items resulting from the purchases, the credit items resulting from the sales, the balance to the debit of petitioner's account as a result of the respective purchases and sales and the debit balances on Januaary 1, 1928, and at the end of each month in that year.

Wherefore, petitioner prays that the board redetermine [fol. 20] petitioner's net taxable income for the year 1928 and redetermine petitioner's deficiency if any in respect of income tax for the said year in such amount as may be established by law or determine that there is no deficiency for said year.

John A. Snyder, Petitioner, by (Sgd.) Harry A. Fellows, Attorney, Union Trust Building, Washington, D. C. (Sgd.) Henry M. Ward, Counsel, Washington, D. C.

Duly sworn to by John A. Snyder. Jurat omitted in printing.

[fol. 21] EXHIBIT "A" TO AMENDED PETITION

Treasury Department, Washington

Office of Commissioner of Internal Revenue

Jun. 6, 1930.

Mr. John A. Snyder,
c/o W. H. MacDade, 607 Bankers Trust Building,
Philadelphia, Pennsylvania.

SIR:

You are advised that the determination of your tax liability for the year 1928 disclosed a deficiency of $38,961.22 as shown in the statement attached.

In accordance with section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned.

Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter you may petition the United States Board of Tax Appeals for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this agreement will expedite the closing of your return(s) by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the enclosed agreement, or on the date assessment is [fol. 22] made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiency.

Respectfully, Robt. H. Lucas, Commissioner; by (Sgd.) David Burnet, Deputy Commissioner.

Enclosures: Statement, Form 882, Form 870.

Statement

IT:AR:B-6. JMF-60D.

Jun. 6, 1930.

In re Mr. John A. Snyder, c/o W. H. MacDade, 607 Bankers Trust Building, Philadelphia, Pennsylvania

Tax Liability

Year	Corrected tax liability	Tax previously assessed	Deficiency
1928	$38,961.22	None	$38,961.22

The report of the internal revenue agent in charge at Philadelphia, Pennsylvania, has been reviewed and approved by this office.

Income reported	$5,352.60
Statutory loss reported	(59,206.99)
Net loss reported	($53,854.39)

Add:

1. Sale of securities	$192,143.25	
2. Statutory net loss reported	(59,206.99)	
Total increase		251,350.24
Ordinary net income adjusted		$197,495.85

[fol. 23] Explanation of Changes

1. The increase in profit from sale of stock is caused by using the method prescribed by article 58, Regulations 74 as follows:

"When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of lots cannot be determined, the stock shall be charged against the earliest purchase of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain * * *."

Inasmuch as the shares sold cannot be identified the profit must be computed as outlined above.

2. The net loss claimed from the year 1926 has been disallowed inasmuch as it was not shown conclusively that you were engaged in a business regularly carried on as defined in article 651, Regulations 74. The internal revenue agent has therefore been sustained in denying your protest.

Computation of Tax

Net income adjusted		$197,495.85
Less:		
Dividends	$33,363.55	
Personal Exemption	3,500.00	
		36,863.55
Balance subject to normal tax		$160,632.30
Normal tax at 1½% on $4,000.00		60.00
Normal tax at 3% on $4,000.00		120.00
Normal tax at 5% on $152,632.30		7,631.62
Surtax on $197,495.85		31,159.17
Total		$38,970.79

[fol. 24] Less:

Earned income credit	9.57
Tax Liability	$38,961.22
Previously assessed	None
Deficiency	$38,961.22

Payment should not be made until a bill is received from the collector of internal revenue for your district and remittance should then be made to him.

[fol. 25]

EXHIBIT "B" TO AMENDED PETITION

C. Clothier Jones & Company

Summary Statement by Months of Purchases and Sales of U. G. I. Stock, Dates, Numbers of Shares Bought and Sold, Prices and Debit Balances

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
Jan.	1	2300							218,696.95
	31	2300							217,422.11
Feb.	6				200	113		2,2546	194,876.11
	9				200	112		2,2346	172,530.11
	29	1900							173,345.91
March	9		100	117			11,725		
	9		100	117			11,725		196,795.91
	12		100	118¾			11,900		208,695.91
	21		100	120			12,025		220,720.91
	31	2300							221,673.62
April	2		100	124			12,425		
	2		100	122			12,225		246,323.62
	10		100	126			12,625		258,948.62
	11		100	128			12,825		271,773.62
	16		100	131			13,125		
	16		100	134⅝			13,487.50		298,286.12
	30	2900							297,478.07
May	3		100	137			13,725		311,203.07
	7		100	146⅛			14,637.50		
	7		100	144			14,425		
	7		100	140			14,025		
	7		100	142¼			14,250		368,540.57
	8		100	148			14,825		383,365.57
	10				100	145		14,473	
	10				100	144⅝		14,435.50	
	10				100	144⅝		14,435.50	
	10				100	144½		14,423	
	10				100	144⅞		14,460.50	
	10				100	145		14,473	
	10				100	145		14,473	
	10				100	144⅞		14,460.50	
	10				100	145		14,473	
	10				100	145		14,473	238,785.57
	14		100	147¾			14,800		
	14		100	148¼			14,850		
	14		100	148½			14,850		
	14		100	148¼			14,850		

EXHIBIT "B" TO AMENDED PETITION—Continued

[fol. 26]

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
May	14		100	147¼			14,750		312,885.57
	18				100	142		14,173	
	18				100	142		14,173	284,539.57
	23				100	140		13,973	
	23				200	140¼		27,996	242,570.57
	31	2500							244,035.16
June	12				100	139		13,873	
	12				100	138		13,773	216,389.16
	13				100	132⅜		13,248	
	13				100	132⅛		13,223	
	13				100	136½		13,660.50	
	13				100	134¾		13,448	
	13				100	136		13,573	
	13				100	131¼		13,098	136,138.66
	14		100	133⅛			13,362.50		
	14		100	133⅛			13,362.50		
	14		100	135½			13,575		
	14		100	134½			13,475		189,913.66
	15		100	138½			13,850		
	15		100	137½			13,775		217,538.66
	15		100	138½			13,875		231,413.66
	18		100	139			13,925		245,338.66
	30	2500							246,721
July	31	2500							245,801.65
Aug.	31	2500							247,839.02
Sept.	29	2500							249,491.28
Oct.	8		500	140¾			70,500		319,991.28
	22				100	146⅛		14,585.50	
	22				100	146		14,573	
	22				100	146½		14,623	
	22				200	145½		29,046	244,663.78
	31	2500							248,528.14
Nov.	5		400	146½			58,700		
	5		100	146½			14,675		319,003.14
	16		100	161¾			16,200		
	16		100	161¾			16,200		
	16		100	161¾			16,200		
	16		100	161¾			16,200		
	16		100	161¾			16,200		403,403.14
	30	3500							405,642.94
Dec.	10				100	152⅛		15,185.50	
	10				100	152⅛		15,185.50	

[fol. 27]

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
Dec.	10				100	152⅛		15,185.50	360,086.44
	11				100	151		15,073	
	11				100	152		15,173	329,840.44
	13		100	157¼			15,750		345,590.44
	26		100	159			15,925		
	26		100	162			16,225		
	26		100	160½			16,075		
	26		100	158			15,825		409,640.44
	31	3500							407,294.70

EXHIBIT "C" TO AMENDED PETITION

MacDonald & Company

Summary Statement by Months of Purchases and Sales of U. G. I. Stock, Dates, Numbers of Shares Bought and Sold, Prices and Debit Balances

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
Jan.	1	3000							283,168.64
	16		100	116½			11,675		280,131.14
	31	3100							293,166.97
Feb.	6				200	113		22,546	270,620.97
	9				200	112		22,346	248,274.97
	29	2700							249,426.36
March	9		200	115⅞			23,225		272,651.36
	12		100	118¾			11,900		284,551.36
	12		100	120½			12,075		296,626.36
	31	3100							297,938.74
April	2		100	122½			12,275		
	2		100	124½			12,475		322,688.74
	10		100	126½			12,675		335,363.74
	11		100	128¾			12,900		349,263.74
	16		100	131			13,125		
	16		100	134			13,425		372,813.74
	30	3700							374,487.54
May	3		100	137			13,725		388,212.54
	7		100	140			14,025		
	7		100	142			14,225		
	7		100	144			14,425		
	7		100	146			14,625		445,512.54
	8		100	148			14,825		460,337.54

[fol. 28]

May	10				800	144¾			
	10				200	144⅝		144,267.50	316,070.04
	11				500	146		72,865	243,205.04
	14		300	147½					
	14		100	147⅝					
	14		100	147¼			73,837.50		317,042.54
	25		200	145½			29,150		346,192.54
	31	3500							347,968
June	12				100	139		13,873	334,095
	12				100	138		13,773	320,322
	13				100	136⅞		13,660.50	
	13				100	132½		13,223	
	13				100	132⅞		13,260.50	
	13				100	136		13,573	
	13				100	134¾		13,448	
	13				100	131½		13,123	240,034
	14		200	134⅝			26,975		
	14		100	135½			13,575		280,584
	15		100	137½			13,775		
	15		200	138¼			27,700		322,059
	18		100	139			13,925		
	18		100	138¾			13,900		349,884
	21				500	133		66,365	283,519
	29		200	135⅞			27,225		311,244
	30	3200							313,113.25
July	2		200	137			27,450		340,563.25
	5		100	138			13,825		354,350.75
	31	3500							353,152.96

EXHIBIT "C" TO AMENDED PETITION—Continued

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
Aug.	31	3500							355,433:73
Sept.	14				800	142¾			
	14				100	143½			
	14				100	143⅞		142,667.50	212,766.23
	30	2500							215,013.78
Oct.	3		1000	141			141,250		356,263.78
	31	3500							356,041.50
Nov.	8		500	156½			78,375		434,416.50
	21		500	168			84,125		518,541.50
	30	4500							521,375.08
Dec.	31	4500							525,527.97

[fol. 29] BEFORE U. S. BOARD OF TAX APPEALS

ANSWER TO AMENDED PETITION—Filed April 24, 1933

Come now the Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, and for answer to the amended petition filed in the above-entitled appeal, admits and denies as follows:

I. Admits the allegations contained in paragraph I of the amended petition.

II. Admits the allegations contained in paragraph II of the amended petition.

III. Admits the allegations contained in paragraph III of the amended petition.

IV. Denies the allegations of error contained in subparagraphs (a) to (d), inclusive, of paragraph IV of the amended petition.

V. Admits the allegations contained in paragraph V of the amended petition, except that the respondent specifically denies that the petitioner was, during the year 1928, engaged in any trade or business other than that of Secretary of the Mechanics Insurance Company at Philadelphia, Pennsylvania, and further specifically denies that the brokerage accounts carred and maintained by the petitioner during said year constituted a trade or business within the meaning of any provision of the Revenue Act of 1928.

VI. Admits the allegations contained in paragraph VI of the amended petition.

[fol. 30] VII. Admits the allegations contained in paragraph VII of the amended petition.

VIII. Admits the allegations contained in paragraph VIII of the amended petition.

IX. Denies the allegations contained in paragraph IX of the amended petition.

X. Denies the allegations contained in paragraph X of the amended petition.

XI. Admits the allegations contained in paragraph XI of the amended petition.

XII. Admits the allegations contained in paragraph XII of the amended petition.

XIII. Admits the allegations contained in paragraph XIII of the amended petition.

XIV. Admits the allegations contained in paragraph XIV of the amended petition, except that the respondent specifically denies that the transactions between the petitioner and the stock brokers during the year 1928 in the purchase and sale of U. G. I. stock were made for the purpose of strengthening petitioner's position in the stock market, increasing his margin of "paper profit" and thereby enabling him to increase his holdings and occupy the position which is commonly known as being "long" on the stock market, as alleged in said paragraph XIV thereof.

XV. Admits the allegations contained in paragraph XV of the amended petition.

XVI. Admits the allegations contained in paragraph XVI of the amended petition.

[fol. 31] XVII. Denies the allegations contained in paragraph XVII of the amended petition.

XVIII. Denies the allegations contained in paragraph XVIII of the amended petition.

XIX. Denies the allegations contained in paragraph XIX of the amended petition.

XX. Admits the allegations contained in paragraph XX of the amended petition.

Denies generally each and every allegation contained in the amended petition not hereinbefore specifically admitted, qualified or denied.

Wherefore, it is prayed that petitioner's appeal be denied.

(Signed) C. M. Charest, General Counsel, Bureau of Internal Revenue. Of Counsel: R. W. Wilson, Special Attorney, Bureau of Internal Revenue.

[fol. 32] BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 49721

Promulgated September 14, 1933

JOHN A. SNYDER, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Where petitioner bought and sold stock without identifying the particular lots, gain or loss on sales is to be computed on the basis of the cost of the earliest purchases. John A. Snyder, 20 B. T. A. 778; affd., 54 Fed. (2d) 57.

Henry M. Ward, Esq., and Harry A. Fellows, Esq., for the petitioner.

R. W. Wilson, Esq., and W. W. Kerr, Esq., for the respondent.

OPINION—Entered September 14, 1933

ARUNDELL:

The respondent's determination of a deficiency in income tax in the amount of $38,961.22 for the year 1928 arises out of his application of the rule of "first in, first out" to sales of stock made by Petitioner in the taxable year.

The facts upon which the case was submitted are those alleged in the amended petition and admitted in the re-

spondent's answer thereto, and those which it was stipulated the petitioner would testify to if present. For the [fol. 33] purposes of this report the pertinent facts may be briefly summarized.

In 1928 and several prior years petitioner dealt in stock of the United Gas Improvement Co. He traded through two brokerage houses on margin and pyramided his purchases. Upon a decline in the market so that his margin fell below the required percentage the brokers reduced his debit balance by sufficient sales to make up the deficiency in the margin. Upon a rise in the market the paper profits were used to increase his holdings of the stock. By this method of operation the stock standing to petitioner's credit on the brokers' books increased during the year from 5,300 shares to 8,000 shares, an increase of 2,700 shares. At the same time his debit cash balance on the brokers' books increased from $501,865.59 to $932,822.67, an increase of $430,957.08. These changes were the result of sales by the brokers at various dates throughout the year of a total of 7,900 shares and the purchase of 10,600 shares for petitioner's account. Purchases and sales affecting petitioner's account were entirely through the medium of street certificates handled by the brokers, who debited and credited petitioner's account to reflect the transactions, and at no time during the year did the brokers, on the one hand, or petitioner, on the other, deliver to each other actual stock certificate.

The substance of petitioner's testimony, offered by stipulation, was that in each case where a sale was made it was his intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount in order to increase his margin and acquire additional shares of the stock.

In determining the deficiency the respondent applied to petitioner's stock transaction the method of computation prescribed by article 58 of Regulations 74, as follows:

[fol. 34] When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots can not be determined, the stock sold shall be charged against the earliest purchases of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain.

The applicability and validity of the above article of the regulations, commonly known as the rule of "first in, first out," are the only questions presented for decision. The same petitioner was before us in a proceeding reported at 20 B. T. A. 778, contesting a deficiency arising out of similar transactions in the same stock in the year 1925. In that case we sustained the respondent's application of the rule in controversy here, and on appeal by the petitioner our decision was affirmed by the Circuit Court of Appeals, Third Circuit, in an opinion reported at 54 Fed. (2d) 57. In the opinion of the Board it was said that there was no evidence of "petitioner's intention to sell any designated stock." Evidently to meet this situation petitioner's testimony was given in this case to the effect that in each sale he intended to sell the most recently acquired stock. This, however, does not establish that the sales were made in that order, and we are unable to find that they were so made in view of the stipulated facts that there were no deliveries of stock certificates, and the transactions were entirely through the medium of street certificates which were not identified or in any way earmarked for petitioner's account. Consequently, the facts upon which we have to go here are in no way different (save as to amounts) from those in the previous case.

Petitioner's principal argument is that the regulation applied here is invalid, under the decision in Heiner v. Donnan, 285 U. S. 312, which was decided since the previous case involving this same taxpayer. The Donnan case dealt [fol. 35] with a conclusive presumption; hence, it involved an entirely different question and is readily distinguishable from this case, in which the presumption is rebuttable. "A rebuttable presumption clearly is a rule of evidence" (Heiner v. Donnan, supra), and "casts upon the person against whom it is applied the duty of going forward with his evidence on the particular point to which the presumption relates." Manley v. Georgia, 279 U. S. 1. It does not estop the taxpayer from establishing the existence of a fact. Where the taxpayer identifies the stock traded in the presumption does not apply. Howbert v. Penrose, 38 Fed. (2d) 577; Cleveland Trust Co., Executor, 24 B. T. A. 132. The presumption announced in the regulations merely follows the rule that has been in effect at least since the decision in Towne v. McElligott (decided in 1921), 274

Fed. 960; hence, it cannot be said to work any hardship on the taxpayer, inasmuch as he had ample warning of the necessity of putting his accounts in shape to enable him to identify his purchases and sales.

Decision will be entered for the respondent.

[fol. 36] Before U. S. Board of Tax Appeals

Decision—Entered September 16, 1933

Pursuant to the Board's opinion promulgated September 14, 1933, it is

Ordered and decided, That there is a deficiency in income tax for the year 1928 in the amount of $38,961.22.

(Sgd.) Eugene Black, Member.

In United States Circuit Court of Appeals

Petition for Review of a Decision of the United States Board of Tax Appeals—Filed December 5, 1933

To the Honorable the Judges of the United States Circuit Court of Appeals for the Third Circuit:

Now comes John A. Snyder, petitioner, by his attorney and counsel and brings this his petition for review of the order of redetermination made by the United States Board of Tax Appeals September 14, 1933 (Docket No. 49721) and shows to the Court as follows:

I. Jurisdiction. The petitioner is a resident of Philadelphia, Pennsylvania, within the Third Judicial Circuit. The return was filed with the Collector of Internal Revenue at the city of Philadelphia.

II. Nature of Controversy. The question presented is one of law upon conceded facts, namely in what amount [fol. 37] petitioner is liable to a deficiency assessment of income tax for the year 1928 upon a profit claimed by the Commissioner to have been realized as a result of certain operations of purchase and sale of shares of stock in the stock market through and by means of margin accounts with stock brokers by the process commonly known as

"pyramiding." The petitioner claims that the net taxable income on which the tax should be computed is $6,308.55 and that the correct amount of the deficiency is $1,896.47. The Commissioner claims that the net income is $197,495.85 and that the tax liability is $38,961.22. The Board of Tax Appeals sustained the ruling of the Commissioner.

III. Record before the Board. The case was submitted to the Board of Tax Appeals upon an amended petition in which the facts were fully set forth, an answer which admitted all but a few of the facts alleged, and a statement of facts proving the facts at issue, received by stipulation in lieu of testimony. No oral evidence was offered by either party.

IV. Questions of Law Presented. The case involves:

First. The applicability to the petitioner's operations on the stock market, for the year 1928, which constituted a trade or business regularly carried on for profit, of the rule of "first in first out" (Article 58, Regulations 74) whereby the results of the transactions for the tax year are disregarded and transactions in prior years examined, in violation of the intent of Congress and rulings of the courts that the transactions of each tax year should be considered separately.

Second. If applicable, the power of the Commissioner in view of the terms of the statute to make and enforce this [fol. 38] rule with respect to petitioner's operations.

Third. If applicable, whether the regulations, as applied to and enforced against petitioner, is not void, under the authority of Heiner v. Donnan, 285 U. S. 312, in that an arbitrary and irrebutable presumption is thereby established which makes it impossible for petitioner to establish the facts by testimony and has the effect of a conclusive presumption.

V. Statement of Facts. On January 1, 1928, petitioner was "long" 5300 shares of United Gas Improvement Co. stock, known as "U. G. I.", which he had acquired in prior years. His debit cash balance on the broker's books was then $501,865.59. In 1928 the brokers sold on various dates 7,900 shares, and bought 10,600 shares, of U. G. I. Petitioner's debit balance was increased to $932,822.67, an increase of $430,957.08. All purchases and sales were made

for petitioner's account by his brokers in the form of street certificates. There was no delivery of certificates between the brokers and petitioner. The certificates of U. G. I. bought by the brokers for petitioner's account, were mingled with thousands of other street certificates of U. G. I. and other stocks and pledged by the brokers with various banks for loans. The petitioner did not at any time own any specified certificates and had no title to or ownership of any certificates. The brokers were under no obligation to hold for petitioner's account any of the certificates bought for his account, and, when they sold U. G. I. on petitioner's orders, they were free to and did deliver any available certificates for a like number of shares, out of lots held for any of their other customers. The petitioner had the right, on payment of an aliquot amount of his debit balance, to de- [fol. 39] mand delivery of so many shares of U. G. I., but the brokers could then deliver any conveniently available street certificates, whether originally purchased for the account of petitioner, or of any other customer. There was no way of identifying any of the certificates while held by the brokers, either those first acquired, those last acquired, or those acquired at any time. The brokerage business on the stock exchanges has always, with respect to margin accounts, been conducted on this basis, and, if the certificates purchased and sold on margin for the thousands of customers were specifically identified and allocated to particular customers the brokerage business could not be carried on. It was petitioner's intention throughout 1928 to accumulate as many additional shares of U. G. I. as market conditions might permit and he sold only when necessary, either because a fall in current daily quotations had impaired his margin, or because by realizing the "paper profit" on a quick turnover, he could improve his market position. In all instances it was his intention to sell the certificates, the purchase of which had brought about the occasion for the sale, in other words to sell the last acquired stock. It was not petitioner's intention at any time to realize in cash the large paper profits shown by comparison of the purchase price of certificates bought in prior years with the prices realized on sales in 1928, nor would it have been of any benefit to petitioner to make sales on the basis of realizing and withdrawing cash profits. Such profits could not have been withdrawn without impairment

of margin and the income tax applicable would have absorbed a large part of the profits.

[fol. 40] ASSIGNMENT OF ERRORS

The Board of Tax Appeals erred in the following particulars:

1. In holding that upon the facts Article 58, Regulations 74, was applicable to petitioner's trade or business of operating on the stock exchange.

2. In disregarding the result of petitioner's operations in this trade or business for the year 1928.

3. In holding that in computing income tax upon petitioner's operations in such trade or business for 1928 the price paid for shares of stock bought in prior years was controlling in determining whether a profit was realized or a loss sustained with respect to shares sold in 1928.

4. In holding that, in so far as applicable to the transactions here involved, the Commissioner was authorized by law to enforce said Article 58 of Regulations 74.

5. In holding that, if authorized by any Act of Congress, the enforcement of said Article 58 of Regulations 74 did not deprive the petitioner of his liberty and property in violation of the Fifth Amendment of the Constitution of the United States.

6. In holding that upon the conceded facts the determination of the Commissioner should be affirmed.

Wherefore petitioner prays that the order of redetermination of the Board of Tax Appeals be reversed and the tax recomputed in accordance with law and that the record [fol. 41] of proceedings be certified to the Circuit Court of Appeals for the Third Circuit.

Dated December 8, 1933.

Harry A. Fellows, Attorney for Petitioner, Union Trust Building, Washington, D. C. Henry M. Ward, of Counsel, 726 Jackson Place, Washington, D. C.

Duly sworn to by Harry A. Fellows. Jurat omitted in printing.

[fol. 42] In United States Circuit Court of Appeals

Notice of Filing Petition for Review

To E. Barrett Prettyman, Esq., General Counsel, Bureau of Internal Revenue, Washington, D. C.:

You are hereby notified that John A. Snyder, by his attorneys, Harry A. Fellows and Henry M. Ward did, on the fifth day of December, 1933, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Third Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this fifth day of December, 1933.

Harry A. Fellows, Henry M. Ward, Attorneys for Petitioner.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this fifth day of December, 1933.

E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue.

[fol. 43] Before U. S. Board of Tax Appeals

Statement of Evidence—Filed December 13, 1933

The above-entitled cause came on for hearing May 22, 1933, before the Honorable C. Rogers Arundell, Member of the United States Board of Tax Appeals, at Washington, D. C., whereupon the following proceedings were had:

Counsel for the petitioner opened the case and stated that it would be submitted upon the amended petition, the answer and a statement of evidence to be received by stipulation. After this statement the following proceedings were had:

The Member: Are you going to have evidence of the fact that the certificates sold were not the earlier purchases or

are you going to argue that the presumption of the Commissioner is not proper and you are going to indulge in a presumption of your own?

Mr. Ward (counsel for petitioner): No. We offer in evidence this statement here with regard to the intention of the taxpayer, and I might read it to your Honor, as this relates to the only allegations of the amended petition which are denied. All of the other allegations are admitted.

The Member: Is this a matter of stipulation between the parties?

Mr. Wilson (counsel for respondent): To the extent that the statement which counsel has prepared and which he is about to offer in evidence represents the testimony which the petitioner would give if he were present, it is admitted that would be his testimony.

The Member: So you are stipulating that. You are not stipulating it is true, but that if present the petitioner would testify to that.

Mr. Wilson: Yes.

[fol. 44] Mr. Ward: That is correct.

Mr. Wilson: The government reserves all objections, of course.

The Member: Has that been signed?

Mr. Wilson: No, your Honor.

Mr. Ward: Shall I read it, your Honor?

The Member: All right.

Mr. Ward: It is agreed that in view of the inability of the petitioner-taxpayer because of illness to attend on the hearing in this case, it is stipulated between the parties that if said John A. Snyder were called as a witness in behalf of petitioner he would testify as follows with respect to the allegations in the amended petition which are denied by the respondent.

Paragraph X. It was the intention of the petitioner throughout the year 1928 to increase his holdings of shares of the United Gas Improvement Company stock in his margin accounts with the stock brokers. In each instance of sale of stock, on the dates and in the amounts specified in the schedules attached to the amended petition and marked, respectively, Exhibits B and C, the respective stock brokers required the petitioner, because of a fall in the market quotations of said U. G. I. stock, either to put up more margin in the form of cash or securities, or to increase

his credit balance by selling a sufficient number of shares of the said stock. In each of such instances petitioner ordered said brokers to sell the various amounts of such stock mentioned in said Exhibits B and C, at the quotations in force on the day of sale, and in each instance petitioner had the intent and purpose of buying back equal or greater amounts of said stock shortly thereafter, according to the market quotations. It was not at any time the petitioner's intention to sell any of the shares of stock purchased in prior years which showed a large paper profit but it was [fol. 45] his intention in each instance of sale on the dates and in the amounts specified in said Exhibits B and C to sell the last acquired stock, the purchase of which followed by the subsequent market fluctuations had brought about an impairment of his margin below the 30 per cent. margin which the brokers required him to maintain. Throughout the year whenever petitioner's cash debit in his account with each of the said brokers was in excess of 70 per cent. of the daily market quotations of the total shares to his credit, he made such sales in accordance with the requirements of the said respective brokers. In all such instances the lack of sufficient margin had been brought about by the debit having been increased through the more recent purchases and through the fall in the market quotations of said stock.

Paragraph XIV. All the transactions in the year 1928 of said brokers in the purchase and sale of U. G. I stock which had the effect of strengthening petitioner's position in the stock market, were made for that purpose and for the purpose of increasing his margin of "paper profit" and thereby enabling him to increase his holdings and occupy the position commonly known as "long" on the stock market.

Paragraph XIX. With respect to each of the items of sale of shares of stock specified in Exhibits B and C it was petitioner's intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount, in order to increase his margin and to enable him through purchases made by said brokers to go "long" of additional shares of said stock, with the hope and expectation, on a further rise in the market, of selling all or a large part of his shares of said stock at a great profit. Throughout 1928 the petitioner did not intend to make any large profits

computed by reference to the purchase price of the shares of said stock acquired in prior years and the sale price of an equal number of shares in 1928 nor, if such profits had [fol. 46] been made, could they have been withdrawn in cash without impairing petitioner's margin and thereby necessitating the sale of additional shares.

The respondent will, upon the hearing, raise such objections to any and all of the above testimony as may seem to him advisable.

The Member: If he had drawn out nothing, what then?

Mr. Ward: He would have had to sell the stock or else put up more margin.

The Member: Is this the completed case; is it submitted now; you have no testimony to put in?

Mr. Wilson: No, sir.

Mr. Ward: Nothing further.

The Member: We will close the record on the testimony.

No other evidence was offered by either party and the case was submitted to the Board on a brief filed by the petitioner.

The foregoing statement of evidence is hereby approved and it is stipulated that the same may be examined and approved by the proper member of the Board of Tax Appeals without notice.

December 7, 1933.

Harry A. Fellows, Attorney for Petitioner; Henry M. Ward, of Counsel. E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue.

The foregoing statement of evidence examined and approved this thirteenth day of December, 1933.

(Sgd.) C. Rogers Arundell, Member, Board of Tax Appeals.

[fol. 47] Before U. S. Board of Tax Appeals

Præcipe for Transcript of Record—Filed December 20, 1933

To the Clerk of the Board of Tax Appeals:

Sir:

You are requested to make a transcript of the record to be filed in the United States Circuit Court of Appeals for

the Third Circuit at Philadelphia, Pennsylvania, pursuant to the petition for review filed herein and to include in such transcript copies of the following documents, duly certified as correct:

1. Docket entries of proceedings before the Board.
2. Amended petition, filed March 22, 1933.
3. Answer to amended petition, filed April 24, 1933.
4. Statement of evidence as settled.
5. Opinion of the Board filed September 14, 1933.
6. Order of redetermination filed September 14, 1933.
7. Petition for review with proof of service.
8. This præcipe.

Respectfully, Harry A. Fellows, Attorney for Petitioner; Henry M. Ward, of Counsel.

We acknowledge service of the foregoing præcipe this twentieth day of December, 1933.

E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue.

[fol. 48] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 49] Minute entry of argument and submission, May 2, 1934, omitted in printing.

[fol. 50] In United States Circuit Court of Appeals for the Third Circuit

March Term, 1934

No. 5419

John A. Snyder, Petitioner,

v.

Commissioner of Internal Revenue, Respondent

On Petition for Review from the United States Board of Tax Appeals

Before Woolley, Davis and Thompson, Circuit Judges

Opinion—Filed September 18, 1934

Woolley, Circuit Judge:

The Commissioner of Internal Revenue found a deficiency tax against Snyder arising out of marginal transac-

tions in the year 1928 which were similar in character to marginal transactions of the same taxpayer in 1925 on which this court passed in Snyder v. Commissioner, 54 Fed. (2d) 57. The Commissioner claims the decision in that case is res judicata of the matter raised on the present petition. Although the law may be the same, the facts, though similar, are different and, being different, they were not passed upon in that case. We hold against the Commissioner's contention of res judicata.

From the deficiency tax assessed by the Commissioner in the instant case, reckoned by setting off the last sales of [fol. 51] shares of stock against shares earliest purchased, Snyder appealed to the United States Board of Tax Appeals. That tribunal discussed in its opinion two questions: one, the validity of Article 58 of Regulations 74 promulgated under the Revenue Act of 1928; the other, the applicability of the regulation to the facts of this case. Snyder is here on petition to review the Board's order sustaining the tax assessed by the Commissioner.

The regulation whose validity is challenged is in these words:

"When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots can not be determined, the stocks sold shall be charged against the earliest purchases of such stock. * * * "

The validity of this regulation, and of like ones under previous statutes, now, for brevity, called the "First in, first out" rule, has repeatedly been sustained by this court and other courts. Snyder v. Commissioner, 54 Fed. (2d) 57; Commissioner v. Merchants and Manufacturers Fire Insurance Company, — Fed. (2d) —; Skinner v. Eaton, Collector, 45 Fed. (2d) 568; Howbert v. Penrose, 38 Fed. (2d) 577, 579.

The usual ground of attack has been that the rule is arbitrary and capricious and therefore in contravention of the due process clause of the Fifth Amendment to the Constitution. This court has held that while the rule is, from the very nature of the situations to which it applies, fixed and peremptory and in that sense arbitrary, it is, from the latitude of its words, not inflexible or capricious and therefore is not unreasonable. Since this pronouncement,

Heiner v. Donnan, 285 U. S. 312, has been decided. On that case the petitioner here takes a new stand. By that decision the Supreme Court held that Section 302 (c) of the Revenue Act of 1926, creating a presumption that gifts [fol. 52] made within two years of the donor's death were made in contemplation of death, was unconstitutional. The petitioner says that the rule which, on failure to identify shares sold, affords a presumption that the shares sold were those first bought is likewise unconstitutional. There is really no analogy between the provision of the statute under consideration by the Supreme Court in the Heiner case and the terms of the rule here under discussion. There the presumption was "conclusive" and made so by the statute. Here the presumption is rebuttable, hence constitutional. Cockrill v. California, 268 U. S. 258, 261; Yee Hem v. United States, 268 U. S. 178, 183-184; Mobile, J. & K. C. R. R. v. Turnipseed, 219 U. S. 35, 42-43. The taxpayer is given every opportunity to identify the shares he has sold and to prove his loss or gain accordingly. Indeed, the rule comes into operation only "when" the identity of the shares sold cannot be determined, which usually happens when the owner in ordering their sale has failed to identify the lots in which they were purchased. In such case there must be some way of determining for the benefit of the taxpayer his losses or gains in his taxable transactions and, similarly, of determining what taxes the government is entitled to exact. Except for this rule or some similar rule, efficiently to administer the revenue act, a vast multitude of potential taxpayers dealing in the purchase and sale of shares on margin and actually making profits would escape taxation because of their inability or disinclination to identify the shares sold and the government would lose the taxes which the statute imposes.

We re-state our judgment that the rule is valid.

The petitioner next contends that the rule, if valid, is not applicable to the instant case because it is inconsistent with the Revenue Act of 1928 which provides (Sections 11, 12, 21, 22 and 23) that there shall be levied, collected and [fol. 53] paid "for each taxable year" normal and surtaxes at certain rates. The substance of this contention is that the annual tax is to be levied and paid only on transactions begun and completed within the "taxable year" and to that end the entire series of the petitioner's marginal transac-

tions in 1928 (the tax year) should be segregated from all transactions in prior years and that transactions of sale in the tax year should be charged only against transactions of purchase in that year, leaving open and unanswered the question how profits from later sales of shares purchased earlier can be taxed. The infirmity in this contention lies in the fact that a transaction of sale of shares previously purchased, yielding a gain, is taxable in the year in which the transaction of sale takes place and the gain is made. 7 R. C. L. Sec. 245. Until the shares, whenever purchased, are sold there is neither gain nor loss. A gain springs from a sale and the tax is imposed on the gain in the year of the transaction of sale. That is the "taxable year". Whether or not there is gain or loss in a sale of shares made in the tax year depends on what shares were sold, the last purchased or the first purchased, or shares intermediate the two, which always is a question answered by the taxpayer's evidence, or by the rule, as to the identity of the shares involved.

We find nothing substantial in this defense.

The petitioner's next position is that the "First in, first out" rule, if valid, is inapplicable to the facts of this case. The facts as stated by the petitioner himself are these:

In 1928 and several prior years the petitioning taxpayer dealt, through two brokerage houses in Philadelphia, in stock of the United Gas Improvement Company known to speculators as U. G. I. through marginal accounts by the process known as pyramiding.

[fol. 54] "On January 1, 1928, (the beginning of the tax year) petitioner was long 5300 shares of U. G. I. During the year 1928 the brokers bought for petitioner's account, on his orders, 10,600 additional shares and sold 7,900 shares. On December 31, 1928 (the end of the tax year) petitioner's account was long 8,000 shares, an increase of 2700 shares for the year. All purchases and sales were in the form of 'street certificates' for 100 shares each endorsed in blank by some brokerage house. They (the certificates) were inextricably mingled with other securities pledged with banks. They (the certificates) were at all times incapable of identification as having been bought or sold for account of petitioner."

"All facts alleged are admitted except in regard to petitioner's intention. His intention (to sell the shares last

bought) was proved at the trial by a statement received in lieu of evidence." (The interpolations are ours.) On these facts, and against the action of the Commissioner in charging the shares sold against shares earliest purchased, the petitioner takes the broad position that the rule in question "is inapplicable to sales of shares of stock in the course of operating on margin accounts, because on its face it assumes sales of shares of stock under circumstances which rendered them capable of identification."

In shorter words, his position is that shares of stock sold on margin are incapable of identification, hence the rule does not apply to such transactions.

From the petitioner's statement of facts and his position on the law, it is obvious he has confused identification of shares and identification of certificates in transactions of sale. The rule deals with the sale and identification of "shares of stock in a corporation," not with sale and identification of certificates. Shares of stock and certificates for shares of stock are different legal entities. Shares of stock "are intangible and rest in abstract legal contempla- [fol. 55] tion". They are the interest or right which the owner has in the management, profits and assets of a corporation. 14 C. J. Secs. 506, 509. Though incorporeal, they nevertheless are property and are the subject of conversion. 14 C. J. Sec. 509; 7 R. C. L. Sec. 166; Skinner v. Eaton, Collector, 45 Fed. (2d) 568. A certificate of stock, on the other hand, is the symbol or paper evidence of the ownership of shares; it is not the stock itself. It is merely written evidence, and then only prima facie evidence, of the ownership thereof by the person designated therein and of the rights and liabilities resulting from such ownership. 14 C. J. Secs. 698, 701, 702, 707, 709, 710, 1043. Howbert v. Penrose, 38 Fed. (2d) 577, 579. A stockholder may prove his ownership of shares by evidence other than that of the certificate, 14 C. J. Sec. 1272; and he may dispose of his shares and surrender his title therein by sale accompanied with delivery of a certificate in his name which he has endorsed with a blank assignment and power of attorney authorizing the transfer. 14 C. J. Secs. 1033, 1050; 7 R. C. L. Secs. 239, 243. As between seller and buyer the shares pass by mere delivery of the certificate, so endorsed, though the transfer as between the new owner and the corporation is not complete until made on the books of the corporation. When the

new owner of the shares sells them without first having them transferred to himself on the books of the corporation and makes delivery by handing over the certificate so endorsed in blank by the original holder and starts it on its wanderings through the "street", the shares may go in one direction and the certificate in another; the shares, however, always being represented (in the rapid shifting of certificates between brokers) by a like certificate in the name of another, with endorsement in blank, held for the owner. Then "ownership follows the owner, not the certificate". Howbert v. Penrose, 38 Fed. (2d) 577, 579. While not technically negotiable instruments, certifi- [fol. 56] cates endorsed in blank pass from hand to hand in the "street" and are regarded in a very extensive practice as quasi negotiable. 14 C. J. Secs. 1033, 1041, 1043, 1044. Upon delivery of a certificate in the seller's name endorsed in blank, or upon delivery of a "street certificate" in the name of someone else, similarly endorsed, the contract of sale between buyer and seller (unless burdened with conditions) is complete and the transfer, within taxing statutes, takes place. 7 R. C. L. Sec. 245.

From these observations, abundantly sustained by decisions, it is plain that the petitioner in this case owned shares of U. G. I. stock, though neither he nor his brokers ever held certificates for them in his name; and, owning them, he had power to sell them when he saw fit and make delivery by certificates, issued to other persons, endorsed by them in blank, and held for him by his broker; and when he sold his shares, as he did, he suffered losses or made gains at the time he sold them. Whether or not there were losses or gains, and in what amounts, depends on what shares he sold and the figures at which they were purchased, that is, whether they were the shares he purchased in 1928, the tax year, or were shares he purchased in prior years. Certainly they were one or the other and he was bound to show that factor in the tax calculation by identifying the shares (as by identifying the "lots" in which they were purchased) both for his own protection in paying and for the protection of the government in exacting taxes. In this and perhaps in other ways the "shares" were "capable of identification". All he showed by way of identifying the shares he sold from "lots" previously purchased was his intention always to sell the shares last

purchased. That may be true, yet he did not transmute his intention into action. He did not order his brokers to sell from any particular lot or otherwise give life to his intention. Skinner v. Eaton, Collector, 45 Fed. (2d) 568, [fol. 57] 569; Howbert v. Penrose, 38 Fed, (2d) 577, 578. He proved what he had thought and also proved that he had done nothing about it. If a taxpayer's intention alone were to govern, it would in every instance be conclusive. Being an operation sealed in his mind, it could not be contradicted by anyone outside. Standing alone as in this case, or "in the absence of something else" as we said in the first Snyder case (54 Fed. (2d) 57, 58), the owner's evidence of his bare intention is not sufficient identification of shares he sold to take the case outside the "First in, first out" rule. On this issue we hold, in accord with our decision in Snyder v. Commissioner, 54 Fed. (2d) 57; Horner v. Commissioner, — Fed. (2d) —; and Commissioner v. Merchants and Manufacturers Fire Insurance Company, — Fed. (2d) —, the deficiency tax assessed against the petitioner must be sustained.

Finally, the petitioner represents that aside from the rule we have been discussing, the transactions which were the subject of the tax in question constituted a trade or business which he regularly carried on, within the meaning of Section 22 of the Revenue Act of 1928 permitting (under Section 23 (e) (1)) deductions for losses so incurred. The petitioner averred in his petition for redetermination of the deficiency tax that during a term of years, including the tax year, "in addition to his regular employment as secretary of an insurance company on salary, (he) was engaged in a business regularly carried on for profit which . . . was the purchase and sale of shares of stock listed on" various exchanges. The Commissioner by his answer denied this averment. At the hearing it was stipulated that if the petitioner were present he would testify to its substance. The Commissioner introduced no evidence in contradiction nor did the Board pass upon the matter in its opinion. Taking the record and the evidence as they stand [fol. 58] we must determine whether there was enough shown to compel the finding which the petitioner asks and to call in play the cited statute.

We cannot find on the petitioner's averment and meager evidence that his case falls within the statute. It is clear

that in certain situations a person who has organized a corporation and invested in its stock and has devoted most of his time to its management may be regarded as having regularly carried on the business and be entitled, under the statute, to make appropriate deductions of stock losses from income. Washburn v. Commissioner, 51 Fed. (2d) 949; Schwinn v. Commissioner, 9 B. T. A. 1304. But lacking convincing evidence of a claimed trade or business regularly carried on, it is generally held that deductions of losses incurred in trade in a given tax year are limited to losses incurred in the actual business of the taxpayer as distinguished from isolated transactions, and do not include losses sustained through dealings on an exchange by one engaged in another business. Mente v. Eisner, 266 Fed. 161; Washburn v. Commissioner, 51 Fed. (2d) 949. We must assume from the order under review that, notwithstanding the silence of the Board on the subject, it found. that the petitioner was not engaged in the trade or business he averred. This finding on what may be a mixed question of law and fact is, in our opinion, sustained by the record.

The order of the United States Board of Tax Appeals is affirmed.

A true copy.—Teste:

—— ——, Clerk of the United States Circuit Court of Appeals for the Third Circuit.

[fols. 59 & 60] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD TERM

March Term, 1934

No. 5419

JOHN A. SNYDER, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appeal from the United States Board of Tax Appeals

JUDGMENT—Filed Sept. 18, 1934

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof it is now here ordered, adjudged, and decreed by this Court that the order or decree of the said Board of Tax Appeals in this cause be, and the same is hereby affirmed.

Philadelphia, September 18, 1934.

Victor B. Woolley, Circuit Judge.

[File endorsement omitted.]

[fols. 61-70] Petition for rehearing, covering 10 pages, filed Oct. 18, 1934, omitted from this print. It was denied, and nothing more, by order of Oct. 24, 1934.

[Title omitted]

ORDER DENYING PETITION FOR REHEARING—Filed Oct. 24, 1934

And now, to wit, October 24, 1934, after due consideration, the petition for rehearing in the above-entitled case is hereby denied.

Philadelphia, ——.

Victor B. Woolley, Circuit Judge.

[File endorsement omitted.]

[fol. 72] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 73] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed February 4, 1935

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted, and the case is assigned for argument immediately following No. 582.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 39,291. U. S. Circuit Court of Appeals, Third Circuit. Term No. 663. John A. Snyder, Petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed January 23, 1935. File No. 663, O. T., 1934.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. 663

JOHN A. SNYDER, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE.

ON PETITION FOR A WRIT OF CERTIORARI TO REVIEW A JUDGMENT OF THE CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, WHICH AFFIRMED AN ORDER OF THE BOARD OF TAX APPEALS.

PETITION FOR WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF.

HENRY M. WARD,
Counsel for Petitioner,
Washington, D. C.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. ....

JOHN A. SNYDER, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE.

ON PETITION FOR A WRIT OF CERTIORARI TO REVIEW A JUDGMENT OF THE CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, WHICH AFFIRMED AN ORDER OF THE BOARD OF TAX APPEALS.

PETITION FOR WRIT OF CERTIORARI

To the Honorable the Chief Justice and Associate Justices of the Supreme Court:

John A. Snyder, the petitioner above named, by his counsel, respectfully shows to the Court:

JURISDICTION

The jurisdiction of this Court to entertain this proceeding and grant the application is conferred by Section 1003(a) of the Revenue Act of 1926; Chap. 27; 44 Stat. 9, 110; U. S. C. Tit. 26, Sec. 1226. The Circuit Court of Appeals for the Third Circuit affirmed the order of the Board of Tax Appeals September 18th, 1934 (R. 57). Petitioner applied for a rehearing, which was denied October 24, 1934 (R. 69). This petition is filed within three months from the date of entry of the order denying the petition for rehearing. *Morse v. United States*, 270 U. S. 151, 154.

OPINIONS BELOW

The findings and opinion of the Board of Tax Appeals (R. 32-35) are reported in 29 B. T. A. 39. The opinion of the Circuit Court of Appeals (R. 49-56) is reported in 73 Fed. (2d) 5.

QUESTIONS PRESENTED

The applicability, and if applicable, the power of the Commissioner of Internal Revenue to enforce, with respect to the instant case, for the tax year 1928, the rule known as "first in first out" prescribed by Article 58 of Regulations 74 (R. 34) reading as follows:

> "When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots cannot be determined, the stock sold shall be charged against the earliest purchases of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain."

IT IS CONTENDED BY PETITIONER:

(1) That where, as in the instant case, the transactions constitute a trade or business of the taxpayer, and more shares are bought during the tax year than are sold, the Revenue Act of 1926, as construed by this Court, requires

that the results of the transactions during the year, whether resulting in gain or loss shall first be determined. Hence that in applying the rule the transactions for the tax year only should be considered, without regard to transactions in prior years.

(2) That the effect of this regulation, under the decisions of the Circuit Court of Appeals and Board of Tax Appeals in the instant case is to establish an irrebuttable presumption of fact, contrary to the principles stated by this Court in *Heiner v. Donnan*, 285 U. S. 312, and in the decisions of this Court on which that case was based.

(3) That, if the regulation be regarded as merely raising a prima facie inference of fact, this inference was at an end when petitioner proved facts to the contrary.

STATEMENT

These questions arise upon the following facts:

The Petitioner throughout the year 1928 was engaged in operating in the stock market on margin by the method as "pyramiding;" his accounts being carried by two brokerage houses in Philadelphia All the transactions of purchase and sale were in shares of stock of the same corporation, United Gas & Improvement Company, of Philadelphia, commonly known and referred to herein for brevity as "U. G. I." (R. 6-9)* All the purchases and sales were in the form of "street certificates" which are certificates for 100 shares of stock standing in the name of some firm of stockbrokers, members of the Stock Exchange, endorsed in blank. They pass in the "street" with the freedom of currency. (R. 12.)

During the year 1928 in a continuous series of transactions the petitioner, through his brokers, bought 10,600 shares of U.G.I. at a total cost of $1,504,637.50 and sold 7,900 shares for $1,095,304.50. His holdings of U.G.I. stock were thus increased in that year by 2,700 shares. (R. 25-

*Except as otherwise noted, all the allegations of fact in the petition to the Board of Tax Appeals (R. 4-28) are admitted in the answer (R. 29-31). References to the petition only, refer to admitted allegations.

28; *Schedules;* R. 8.) There were 73 transactions of purchase and 50 of sale (R. 25-28).

On the year's transactions petitioner realized an actual profit of about $43,682** on which the tax is $1,897.77. His unrealized "paper profit" (the difference between cost and market value at the end of the year, assumed to be 160) was about $239,500. (Schedules, R. 25-28.)

The allegation that these operations constituted a trade or business (R. 10) is denied (R. 30). It was proved by petitioner's statement received in lieu of evidence (R. 44) and by the schedules of transactions (R. 25-28), showing the volume of the transactions. Under the authorities cited in the supporting brief, these transactions constituted a trade or business.

DETERMINATION OF COMMISSIONER OF INTERNAL REVENUE, BOARD OF TAX APPEALS AND CIRCUIT COURT OF APPEALS.

The Commissioner held that the profit realized during the year *1928* should be determined by deducting from the sales price *realized in that year* the cost of equivalent amounts of shares of U.G.I. stock *acquired in prior years,* wholly without regard to the segregated transactions for the tax year involved. By this method the Commissioner computed the taxable profit on these sales at $192,143.25, nearly 90 per cent of the unrealized "paper profit." (R. 22.)

The action of the Commissioner was upheld by the Board of Tax Appeals (R. 35). The order of the Board was affirmed by the Circuit Court of Appeals (R. 57).

REASONS FOR GRANTING CERTIORARI:

(1) The case presents important questions of Federal Income Tax law which have not been, but should be, settled by this Court, namely,

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**See Appendix B to supporting brief, p. 30, where the tax is calculated from the schedules (R. 25-28).

(a) Whether, where a taxpayer is engaged in the trade or business of trading on the stock exchange, the transactions in the tax year should be segregated and the tax computed on the year's transactions without recourse to prior years.

(b) Whether as applied to such transactions the regulation, approved and enforced by the Court below, is authorized by the Revenue Act of 1928 and other Revenue Acts as construed by this Court.

(c) Whether the Commissioner of Internal Revenue has the power to establish by regulation an irrebuttable presumption of fact which overcomes the only evidence available to taxpayers in similar situations, namely the intention to sell the certificates bought in the tax year and not those bought in prior years.

(2) There is a conflict between the Circuit Court of Appeals for the Third Circuit in the instant case, and the Circuit Court of Appeals for the Fourth Circuit in *Howbert v. Penrose*, 38 Fed. 2d, 577, 578, with regard to the right of the taxpayer to carry out his intention and decision to sell the last acquired shares first.

(3) The Circuit Court of Appeals has decided a Federal question in the instant case, namely the power of the Commissioner of Internal Revenue to establish by regulation an irrebuttable presumption of fact, in a way probably in conflict with applicable decisions of this Court, namely: *Bailey v. Alabama*, 219 U. S. 219, 238; *Manley v. Georgia*, 279 U. S. 1; *Heiner v. Donnan*, 285 U. S. 312, 326, 329; *Mobile & J. K. R. R. Co., v. Turnipseed*, 219 U. S. 35, 41.

The importance of these questions, is emphasized in the Government's petition for certiorari in a parallel case in which the same regulation is involved, No. 582, *Helvering v. Rankin*, now *sub judice*. (Petition filed December 18, Respondent's brief filed January 17.) In that case it is stated in the petition for the writ as follows (pp. 9-10):

"The court below sought to make a distinction between a sale of certificates and a sale of shares. See

also the second *Snyder case, supra*. (The instant case, 73 Fed. (2d) 5). It recognizes that in marginal transactions *certificates cannot be identified*, but holds that *shares, as distinguished from certificates*, are capable of identification. *This so-called distinction does not exist.*"

"The decision below deals with a class of transactions in which a large number of taxpayers engage. * * * Marginal transactions are of common and frequent occurrence. * * * The Treasury Department advises that a large number of cases of this character are now pending in the Bureau. * * * It is important in the administration of the revenue that the proper method of computing gains and losses on this type of transaction should be settled. * * * *It is important*, therefore, *that this Court pass* upon this case and *establish rules to guide the Government and taxpayers* in future cases of this character." (Italics supplied)

It is suggested that the petitions in No. 582 and in the instant case be granted and the two cases heard on the same day.

WHEREFORE, petitioner prays that a writ of certiorari be granted.

HENRY M. WARD,
Counsel for Petitioner,
Washington, D. C.

January 21st, 1935.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

OPINIONS BELOW

Board of Tax Appeals, 29 B. T. A. 39.
Circuit Court of Appeals, 73 Fed. (2d) 5.

JURISDICTION

The jurisdiction is fully stated in the petition, page 2.

STATEMENT

Petitioner throughout the year 1928 was trading on the Philadelphia Stock Exchange. All his transactions were confined to purchases and sales of shares of stock of United Gas & Improvement Company, of Philadelphia, referred to throughout for brevity as "U.G.I." He carried on his operations through two stock exchange houses in Philadelphia. The operations were on margin accounts and additional shares were bought from time to time continuously during the tax year by the method known as "pyramiding." That is to say, the brokers carried several thousand shares of U.G.I. to petitioner's credit and a cash debit of several hundred thousand dollars for the amounts advanced to make the purchases. Petitioner was credited with dividends from time to time and debited with interest on the current cash debit balances. The market was rising throughout the year with occasional relapses. The brokers, as customary, required that the cash debit balance should not exceed at any time 70 per cent of the current daily market quotations of the shares to petitioner's credit. In other words, the brokers required a 30 per cent "margin." (R. 10-11.)

Whenever the cash debit balance exceeded 70 per cent of current quotations the brokers required petitioner either to deposit sufficient cash or securities or to sell sufficient of the shares to his credit to restore his margin. In every in-

stance in the tax year petitioner, for this express purpose, sold a sufficient number of shares of U.G.I. (R. 11, 45.)

Thereafter, on a rising market he bought back an equal or greater number of shares. (R. 9, 15.)

Petitioner's object throughout the year was *to accumulate as many shares of U.G.I. as he could.* (R. 9, 15.) He did not intend or attempt at any time to realize a profit on shares bought in prior years, but intended in every instance of sale in 1928 to sell the shares last bought, the purchase of which had overloaded his account and brought about the requirement for more margin. (R. 10; denied, proved by statement, R. 44.)

On this basis of trading in earlier years petitioner had to his credit January 1, 1928, with the two brokers, 5300 shares of U.G.I. stock bought in prior years and a debit cash balance of $501,866.59. (R. 7, 8, 25, 27.) During the tax year the brokers bought on his order 10,600 additional shares at a total cost of $1,504,637.50 and sold 7,900 shares for $1,095,304.50 (Schedules, R. 25-28). Consequently petitioner had to his credit at the end of the tax year 8,000 shares (an increase of 2,700) and a cash debit balance of $932,822.67 (an increase of $430,956.08).

The operations for the tax year 1928 showed an actual profit of about $43,682 and a tax liability of $1,897.77.* The Commissioner of Internal Revenue, by taking the purchase prices of equal amounts of shares *in prior years* and the *sales prices in 1928,* computed a taxable profit of $192,143.25, on which he computed a deficiency tax of $38,961.22. (R. 22.)

This profit nearly equalled the unrealized paper profit on the year's transactions.

This result was reached by applying the rule of "first in first out" established by Article 58 Regulations 74, which reads as follows:

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*This is an arithmetical computation from the schedules in evidence (R. 25-28) and is stated in detail below. (Appendix B, p. 30.)

> "When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots can not be determined, the stock sold shall be charged against the earliest purchases of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain." (R. 34.)

While the Board of Tax Appeals found certain of the facts, substantially all the facts are admitted in the answer to the amended petition before the Board (Petition, R. 6-17, 19; Schedules, R. 25-28; Answer, R. 25-31). These admitted facts supplement and control the facts found by the Board.

The respondent denied that the petitioner was engaged in any trade or business other than that of secretary of an insurance company and denied that the brokerage accounts constituted a trade or business within the meaning of any provision of the Revenue Act of 1928 (R. 29, par. V). The accuracy of the schedules, showing the transactions in detail, was admitted (Petn. par. XX, R. 19; Schedules R. 25-28; Answer, par. XX, R. 31).

The Court of Appeals held that these transactions did not constitute a "trade or business." (R. 56) The court, however, stated that the allegation that petitioner "was engaged in a business regularly carried on for profit" was covered by the stipulation at the hearing that if the petitioner were present he would testify to its substance. (R. 55.) The court below also held that this is a mixed question of fact and law. (R. 56.) The conclusion that the operations constituted a trade or business is self-evident and follows from the conceded fact that the transactions were continuous throughout the year and involved the purchase of over 10,000 shares at a cost of over a million and a half dollars and sales of 7,900 shares at a price of over a million dollars.

Petitioner was prevented by illness from giving oral tes-

timony. His statement was received in lieu of evidence. (R. 43-46.)

This statement clearly proves his intention to increase his holdings of U.G.I. (R. 45, par. XIX) and to sell the shares the purchase of which, with a fall in daily quotations had impaired his margin (R. 44-45) and to buy back the same, or a greater number of shares, when market conditions permitted. In every instance the petitioner bought back an equal or greater number of shares within a few days (*Schedules*, R. pp. 25-28. Analysis of Schedules, Appendix A, *infra*, pp. 26-29.)

The repurchase of shares, which was continuous throughout the tax year, completely negatives the theory that petitioner was selling the shares acquired in prior years or doing anything else than strengthening his "long" position on the market as is fully proved by his statement (R. 45-46, par. XIX).

ERRORS RELIED ON

The Court below erred:

1. In holding (R. 51) that the principle stated in *Heiner v. Donnan*, 285 U. S. 312, applies only to *conclusive* statutory presumptions; whereas, as clearly appears from the opinion and cited decisions of this Court on which it is based, the principle applies equally to presumptions which, although not in form conclusive, are *in fact* irrebuttable and, therefore, are *in effect* conclusive.

2. In holding (R. 51) that, upon the facts admitted in the pleadings, in the customary course of dealings between stockbrokers and their customers (R. 11-17, pars. XI-XVI):

> "The taxpayer is given every opportunity to identify the shares he has sold and to prove his loss or gain accordingly."

Whereas, as clearly appears from the admitted facts cited, it is not possible to identify any particular shares or certificates in the customary trading operations on the stock exchange on margin accounts.

3. In holding (R. 53-55) that the regulation of "first in first out" applies to "shares of stock in a corporation" and not to *the certificates* of shares, in which alone the dealings were had, and that by giving orders to his "brokers to sell from any particular lot" he would have supplied the necessary identification, whereas upon the conceded facts (R. 14, pars. XII-XIII) the broker would have been under no obligation whatever to sell any particular shares (or certificates) from any particular lot.

4. In holding (R. 53) that upon the conceded facts the brokers were selling, not stock certificates but "shares" owned by petitioner, whereas in every instance "street certificates" were bought and sold, the petitioner did not have title to any particular shares, was not a stockholder, and his only right was to call upon the brokers for the delivery of certificates for so many shares upon paying in cash, or other value, the aliquot debit balance on the broker's books. Petitioner's rights did not in the tax year, ripen into possession or actual ownership of any specified certificates or shares.

5. In holding (R. 58-59) that the volume of the transactions with other evidence did not establish as a conclusion of law that petitioner's operations on the stock exchange constituted a trade or business.

SUMMARY OF ARGUMENT

FIRST: THE DECISIONS OF THIS COURT REQUIRE THAT INCOME TAX SHOULD BE COMPUTED IN THE FIRST INSTANCE WITH RESPECT TO TRANSACTIONS OF PURCHASE AND SALE CONSUMMATED WITHIN THE TAX YEAR, WITHOUT REFERENCE TO PURCHASES IN EARLIER YEARS. (p. 13.)

Burnet v. Sanford & Brooks Co., 282 U. S. 359.
Woolford Realty Co. v. Rose, 288 U. S. 319.

SECOND: PETITIONER'S TRANSACTIONS ON THE STOCK EXCHANGE CONSTITUTED A TRADE OR BUSINESS WITHIN THE MEANING OF SECTION 22 OF THE REVENUE ACT OF 1928. (p. 14.)

Flint v. Stone Tracy Co., 220 U. S. 127, 171.
Washburn v. Commissioner, 51 Fed. (2d) 949 (C. C. A. 8th) and cases cited.
Schwinn v. Commissioner, 9 B. T. A. 1304.

THIRD: THE EXTENSION IN THE INSTANT CASE OF THE RULE OF "FIRST IN FIRST OUT" TO PURCHASES IN PRIOR YEARS IS NOT AUTHORIZED BY THE REVENUE ACT OF 1928 AND IS, THEREFORE, BEYOND THE POWER OF THE COMMISSIONER. (p. 16.)

FOURTH: IT WAS IMPOSSIBLE TO IDENTIFY ANY OF THE SHARES SOLD. HENCE THE REGULATION CANNOT WITH REASON BE APPLIED TO TRANSACTIONS OF THIS NATURE. (p. 18.)

Richardson v. Shaw, 209 U. S. 365, 378-379.
Direction der Disconto Gesellschaft v. United States Steel Corporation, 267 U. S. 22, 28.

FIFTH: THE REGULATION IS BEYOND THE POWER OF THE COMMISSIONER IN ITS APPLICATION TO THE INSTANT CASE IN THAT IT ESTABLISHES AN IRREBUTTABLE PRESUMPTION OF FACT. (p. 21.)

Heiner v. Donnan, 285 U. S. 312, 328.
Manley v. Georgia, 279 U. S. 1, 8.
Western Atlantic R. Co. v. Henderson, 279 U. S. 639, 642.
Bailey v. Alabama, 219 U. S. 219, 238.

SIXTH: THERE IS A CONFLICT BETWEEN THE DECISION OF THE THIRD CIRCUIT COURT OF APPEALS IN THE INSTANT CASE AND THAT OF THE FOURTH CIRCUIT IN *Howbert v. Penrose*, 38 Fed. (2d) 577, 578, ON THE VITAL POINT INVOLVED THAT THE INTENTION OF THE TAXPAYER IS CONTROLLING. (p. 23.)

SEVENTH: THE EVIDENCE OF PETITIONER'S INTENTION IS UNCONTRADICTED AND IS CORROBORATED BY THE TRANSACTIONS SET OUT IN THE RECORD. IT MUST, THEREFORE, PREVAIL OVER THE REGULATION. (p. 24.)

Chesapeake & Ohio R. R. Co. v. Martin, 283 U. S. 209, 215, 216.
Chicago Ry. Equipment Co. v. Blair, 20 Fed. (2d) 10, 12 (C. C. A. 7th).
Mobile J. & K. R. R. Co. v. Turnipseed, 219 U. S. 35, 41.

CONCLUSION: THE PETITION FOR THE WRIT OF CERTIORARI SHOULD BE GRANTED. (p. 25.)

FIRST.

THE DECISIONS OF THIS COURT REQUIRE THAT INCOME TAX SHOULD BE COMPUTED IN THE FIRST INSTANCE WITH RESPECT TO TRANSACTIONS OF PURCHASE AND SALE CONSUMMATED WITHIN THE TAX YEAR, WITHOUT REFERENCE TO PURCHASES IN EARLIER YEARS.

Burnet v. Sanford & Brooks Co., 282 U. S. 359, is the converse of the instant case. In that case the taxpayer (on a cash basis) in 1920, recovered a judgment for $192,577.59 against the United States on certain dredging contracts, which it had performed at a heavy loss in prior years. From this amount the taxpayer deducted the prior losses and returned the balance as taxable income. The Commissioner held the entire amount was taxable income. So did the Board. The Fourth Circuit Court of Appeals sustained the deductions claimed by the taxpayer (35 Fed. (2d) 312).

This Court reversed the Court of Appeals and sustained the Commissioner. At page 363 the opinion by Mr. Justice Stone reads:

> "All the revenue acts which have been enacted since the Sixteenth Amendment *have uniformly assessed the tax on the basis of annual returns showing the net result of all the taxpayer's transactions during a fixed accounting period*, either the calendar year, or at the option of the taxpayer, the particular fiscal year which he may adopt."*

See also to same effect:

Woolford Realty Co. v. Rose, 288 U. S. 319, 326.

*Italics supplied throughout unless otherwise noted.

SECOND.

PETITIONER'S TRANSACTIONS ON THE STOCK EXCHANGE CONSTITUTED A TRADE OR BUSINESS WITHIN THE MEANING OF SECTION 22 OF THE REVENUE ACT OF 1928.

Petitioner's operations on the exchange were continuous throughout the greater part of the tax year. They are stated in detail in Schedules B and C attached to the petition before the B. T. A. (R. 25-28, and in the analysis of those schedules, Appendix A, *infra*, pp. 26-29).

During the tax year petitioner bought through two brokers 10,600 shares of U. G. I. at a cost of $1,504,637.50. He sold 7,900 shares for $1,095,304.50. His long share credit balance was increased, pursuant to his intention to accumulate U. G. I. on a rising market, from 5,000 to 8,000 an increase of 2,700 shares. His debit cash balance was increased from $501,866.59 to $932,822.57, an increase of $430,956.08 (*Schedules*, R. 25-28). In all there were 73 transactions of purchase and 50 of sale, in lots varying from 100 to 1,000 shares at a time, the great bulk in lots of 100. All transactions were in the form of "street certificates;" that is to say, certificates for 100 shares each, in the name of a stock exchange firm, endorsed in blank (R. 12, 14).

Petitioner undertook these operations for profit (R. 6, 17, 19) in order to accumulate as many shares as he could on a rising market using his paper profit as margin (*Ibid.*).

He clearly was not an investor, buying securities outright to derive income from them. All the transactions were speculative and obviously required constant attention to the brokers' requirements for more margin (R. 9-11), and to the daily market fluctuations, in order that, whenever a sale was made, an equal or greater amount of shares might be bought back when permitted by market conditions (R. 10).

In every instance it was petitioner's intention to sell the last acquired stock first (R. 11, 44-45). To sell the stock, the purchase of which had brought about the occasion for and requirement of the sale (*Ibid*).

Under these circumstances it seems clear that within the commonly accepted meaning of the terms "business" and "trade" these operations constituted both. Similar operations are commonly known as "*trading*" on the stock exchange.

In *Flint v. Stone Tracy Co.*, 220 U. S. 107, 171, the opinion quotes with approval the definition of "business" in Bouvier's Law Dictionary, 372, as follows:

> "That which occupies the time, attention and labor of men for the purpose of livelihood or profit;"

and that in Black's Law Dictionary, 158:

> "'Business' is a very comprehensive term and embraces everything about which a person can be employed."

Petitioner is insistent upon the point that the operations constituted a trade or business, or transaction entered into for profit within the statute not in order to deduct losses, but to emphasize the controlling rule (Point First above, p. 13) that the law requires the tax to be computed on the segregated transactions of each year.

While this rule would probably be applicable if the operations did not constitute a business they are *a fortiori* applicable when business transactions are involved and the operations constitute the year's business.

The Commissioner was no more justified in holding by means of the irrebuttable presumption, established by the rule of "first in first out" that the shares sold in 1928 were those bought in prior years at a lower price, than the taxpayer (petitioner) would have been in claiming deductible losses if the shares had been bought in prior years at higher prices than those at which they were sold in 1928. See *Burnet v. Sanford & Brooks Co.*, 282 U. S. 359, *supra*.

THIRD.

THE EXTENSION IN THE INSTANT CASE, OF THE RULE OF "FIRST IN FIRST OUT" TO PURCHASES IN PRIOR YEARS IS NOT AUTHORIZED BY THE REVENUE ACT OF 1928, AND IS, THEREFORE, BEYOND THE POWER OF THE COMMISSIONER.

The Revenue Act of 1928 (45 Stat. 791) in so far as applicable reads as follows:

> "Sec. 11. (45 Stat. 795) There shall be levied, collected and paid *for each taxable year* a normal tax equal to the sum of the following:
>
> "(a) 1½ per centum of the first $4,000 of the amount of the net income in excess of the credits against net income provided in section 25, etc."
>
> "Sec. 12 (Ibid, 796) (a) Rates of surtax—There shall be levied, collected, and paid *for each taxable year upon the net income* of every individual a surtax as follows:" etc.
>
> "Sec. 21 (Ibid, 797) *Net Income.*
>
> "Net income means the gross income computed under Section 22, less the deductions allowed by Section 23.
>
> "Sec. 22. (Ibid) *Gross Income.*
>
> "(a) General definition. 'Gross income' includes gains, profits and income derived from * * * trades, businesses, * * * or sales, or dealings in property * * * growing out of the use of or interest in such property * * * of the transaction of any business carried on for gain or profit."
>
> "Sec. 23. (Ibid, 799) In computing net income there shall be allowed as deductions:—
>
> "(e) Losses by individuals. In the case of an individual, losses, sustained during the taxable year and not compensated for by insurance or otherwise.
>
> "(1) If incurred in trade or business."
>
> "(2)If incurred in any transaction entered into for profit, though not connected with any trade or business."

The words "for each taxable year" in sections 11 and 12 control the definitions of "gross income" and "net income" in sections 21, 22 and 23.

Hence the phrase in Section 22 (a):

> "Gross income includes gains, profits and income derived from trades, businesses * * * or sales or dealing in property" etc.

means the same as if written

> "Gross income includes gains, profits and income derived *for each taxable year* from trades, businesses, etc."

and the phrase in Section 23:

> "In computing net income there shall be allowed as deductions"

means the same as if written:

> "In computing net income *for each taxable year* there shall be allowed as deductions."

Hence the statute with respect to a trade or business or transaction entered into for profit, commands the taxing authority to include in "gross income" the gains and profits derived therefrom for "*each taxable year*" and to allow as deductions:

> "losses sustained *during the taxable year* if incurred in trade or business."

The statute, as emphatically held by this Court in *Burnet v. Sanford & Brooks Co.*, 282 U. S. 359, and *Woolford Realty Co. v. Rose*, 286, U. S. 319 (discussed above First Point, p. 13) requires, as stated in the latter case:

> "the computation of gains and losses on the basis of an annual accounting *for the transactions of the year.*"

Whatever application and validity the regulation may have with respect to an *investor* who has physical possession of a lot of shares acquired in different years and through some carelessness or oversight is unable to identify the shares sold in the tax year, is not the question here

presented. In such case the taxpayer is not, as here, engaged in a trade or business.

The statute does not authorize the Commissioner, in ascertaining the profits of the business "for each taxable year" to be included in gross income and the losses for the same "taxable year" to be deducted, to assume, as has been done in the instant case, that the shares sold in 1928 were those purchased in 1927, 1926, or 1925 and hence that this taxpayer, who in fact on his operations in 1928 made an actual profit of some 43,682, made an imaginary profit of over $192,000.

FOURTH.

IT WAS IMPOSSIBLE TO IDENTIFY ANY OF THE SHARES SOLD. HENCE THE REGULATION CANNOT WITH REASON BE APPLIED TO TRANSACTIONS OF THIS NATURE.

In its operation in the instant case the rule is both arbitrary and oppressive. It is conceded; (a) that all transactions of purchase and sale were in the form of street certificates for 100 shares each, in the name of some stock exchange house endorsed in blank; (b) that the identity of the certificates, and hence of the shares, bought on petitioner's orders was completely lost and such shares were at all times incapable of identification; (c) that the petitioner had no rights in any specified certificate; (d) that his only right was to require the delivery of so many shares on paying the brokers an aliquot amount of his debit balance; (d) that the broker's only obligation was at all times to have available for delivery on payment therefor certificates for the required number of shares. All these facts were in accordance with the well established and usual course of dealing on the stock exchange (R. 11-15, petition to Board, pars XI-XIII).

The facts pleaded and admitted are substantially as stated in *Richardson v. Shaw*, 209 U. S. 365, 378, 379.

In the Government's petition for certiorari in No. 582, *Helvering v. Rankin,* it is stated, referring to margin accounts (R. 6, 7):

> "Particular shares are not identifiable, because the common fund is the common property of all dealing in that stock and this common fund is in a constant state of flux. The regulation was designed to meet just such a condition and provides *for a cost basis* in these transactions where identification is impossible."

In other words (applying the above to the instant case), the Commissioner is justified in making and enforcing a regulation, the result of which, in the instant case, is to increase the tax from about $1,900 on the transactions in the tax year to over $38,000 based on purchases prior to the tax year.

The regulation when applied on a rising market over a period of years results in enormously increasing the taxes.

It is arbitrary and oppressive because it prevents a customer from dealing in the same security over a period of years. In the instant case it happened that the petitioner on January 1st, 1928, was long of U.G.I. and dealt only in U.G.I. during the tax years. His operations might have been precisely the same in 1928 had his credit balance consisted of entirely different securities. Segregating the tax-year, the only thing to be considered was whether the margin was preserved. The U.G.I. stock held on January 1st was merely collateral pledged to secure the debit balance. It might as well have been bonds or any other securities.

Had there been no U.G.I. shares to petitioner's credit on January 1st the profit or loss would necessarily have been computed on the operations in U.G.I. during the tax year. There is no reason in the instant case for an arbitrary regulation relating back to purchases in earlier years.

The Court of Appeals stated (R. 51) in discussing the validity of the regulation:

> "The taxpayer is given every opportunity *to identify the shares he has sold* and to prove his loss or gain accordingly."

In the instant case the petitioner had a well-defined plan of increasing his holdings of U.G.I. To that end he never sold without buying back an equal or greater number of shares.

Apparently the court below thought that if petitioner had made a written memorandum of his intention to sell the last acquired shares first or had given his brokers an order to that effect there would have been an identification, as in the Rankin case (No. 582).

But it is conceded in the instant case and it was held in *Richardson v. Shaw*, 209 U. S. 365 (*supra*) that the broker was under no obligation to carry out such order. All the certificates of U.G.I. were inextricably mixed, the last acquired with the first.

It follows that a memorandum, book entry or order would have been *merely evidentiary of petitioner's intention* and in the instant case would have added nothing of substance to his clear statement of this intention, corroborated by the transactions in detail (R. 44-45; 25-28).

The attempted distinction made by the Court of Appeals (R. 53) between "shares" and "certificates" is not justified by the facts and is subject to the criticism of being metaphysical. It is asserted in the Government's petition for certiorari in the *Rankin* case (No. 582) that the attempted distinction is unsound. At page 9 this petition reads:

> "The court below sought to make a distinction between a sale of certificates and a sale of shares. See also the second *Snyder case, supra.* It recognizes that in marginal transactions certificates cannot be identified, but holds that shares, as distinguished from certificates are capable of identification. *This so-called distinction does not exist.*"

Moreover the attempted distinction is inconsistent with the opinion of this Court in *Direction der Disconto Gesellschaft v. United States Steel Corporation*, 267 U. S. 22, 28.

FIFTH.

THE REGULATION IS BEYOND THE POWERS OF THE COMMISSION IN ITS APPLICATION TO THE INSTANT CASE, IN THAT IT ESTABLISHES AN IRREBUTTABLE PRESUMPTION OF FACT.

It has been shown above that the only evidence available to petitioner—or to any other taxpayer trading actively on margin accounts—was that of his intention. This evidence is corroborated by the transactions in the record—yet the Board (R. 35) and the Court of Appeals (R. 51) held that *Heiner v. Donnan*, 285 U. S. 312 is not in point, because in that case the statutory presumption was denominated "conclusive." Both the Board and the Court demoninated the rule of first in first out "rebuttable" and therefore sustained it.

It is submitted that in so ruling they wholly disregarded the reasoning of this Court and the theory upon which, as shown by the cases cited in the opinion, that case was decided.

Heiner v. Donnan, 285 U. S. 312, deals with a conclusive presumption created by a Federal taxing statute. The statute was held void because the conclusive statutory presumptions, that every gift made by a decedent within two years of death was in contemplation of death, made it impossible for the taxpayer to show by evidence that in fact the gift was not in contemplation of death. In reaching this conclusion this Court held that the restraint upon Federal legislation by the due process clause of the Fifth Amendment is the same as that upon State legislation by the Fourteenth Amendment.

On this point the opinion at page 326 reads:

> "Nor is it material that the Fourteenth Amendment was involved in the *Schlesinger* case, instead of the

Fifth Amendment, as here. The restraint imposed upon legislation by the due process clauses of the two amendments is the same. *Coolidge v. Long*, 282 U. S. 582, 596."

The ruling that the conclusive presumption was void, was based upon decisions of this Court in which *prima facie statutory presumptions in State statutes* were held to be void because *their effect was to prevent the litigant from proving the facts*—in other words these statutory presumptions were held void because *irrebuttable*, precisely the situation in the instant case.

On this point the opinion reads (p. 329):

"This court has held more than once that a statute *creating a presumption which operates to deny a fair opportunity to rebut it* violates the due process clause of the Fourteenth Amendment. For example, *Bailey v. Alabama*, 219 U. S. 238; *et seq.*; *Manley v. Georgia*, 279 U. S. 1, 5-6. 'It is apparent', this court said in the *Bailey* case (p. 239) 'that a constitutional prohibition *cannot be transgressed indirectly* by the creation of a statutory presumption any more than it can be violated by direct enactment. The power to create presumptions is not a means of escape from constitutional restrictions.'"

In *Manley v. Georgia*, 279 U. S. 1, 6, the opinion reads:

"A *prima facie* presumption casts upon the person against whom it is applied the duty of going forward with his evidence on the particular point to which the presumption relates. A statute creating a presumption that is arbitrary or *that operates to deny a fair opportunity to rebut it* violates the due process clause of the Fourteenth Amendment. *Bailey v. Alabama*, 219 U. S. 219, 233 *et seq.* *Mere legislative fiat may not take the place of fact in the determination of issues involving life, liberty or property.*"

Followed in *Western & Atlantic R. Co. v. Henderson*, 279 U. S. 639, 642, which held to be invalid a State statute which

created a presumption of negligence against railroad companies

> "unless the company shall make it appear that their agents have exercised all ordinary and reasonable care and diligence, the presumption in all cases being against the company."

In *Bailey v. Alabama*, 219 U. S. 238, the opinion reads:

> "The latest expression upon this point is found in the case last cited (*Mobile, J. & K. C. R. R. Co. v. Turnipseed*, 219 U. S. 35) where the court, by Mr. Justice Lurton said: 'That a legislative presumption of one fact from another may not constitute a denial of due process of law or a denial of the equal protection of the law it is only essential that there shall be some rational connection between the fact proved and the ultimate fact presumed and that the inference of one fact from proof of another shall not be so unreasonable as to be a purely arbitrary mandate. So also it must not, *under guise of regulating the presentation of evidence, operate to preclude the party from the right to present his defense to the main fact thus presented.*'"

SIXTH.

THERE IS A CONFLICT BETWEEN THE DECISION OF THE THIRD CIRCUIT COURT OF APPEALS IN THE INSTANT CASE AND THAT OF THE FOURTH CIRCUIT IN *Howbert v. Penrose*, 38 FED. (2D) 577, 578, ON THE VITAL POINT INVOLVED, THAT THE INTENTION OF THE TAXPAYER IS CONTROLLING.

On this point the opinion of the Court of Appeals in *Howbert v. Penrose* (p. 578) approves and quotes the opinion of the District Judge, in which it is stated:

> "Where a party has held stock for many years and later buys more, and in this case it is admitted that plaintiff bought a great deal more after 1913 than he sold in 1918, *he has a right to decide which stock he is going to sell.* The Government has not the power to say that if the taxpayer sells any of his holdings in a

particular company, *it can say conclusively that he sold the stock bought at the cheapest price* or *the shares purchased before or* after a *certain date. He has the right to decide that himself.*"

SEVENTH.

THE EVIDENCE OF PETITIONER'S INTENTION IS UNCONTRADICTED AND IS CORROBORATED BY THE TRANSACTIONS SET OUT IN THE RECORD. IT MUST, THEREFORE, PREVAIL OVER THE REGULATION.

As pointed out in the instant case the intention of the taxpayer as to whether the certificates sold are those last purchased is necessarily controlling. It is for him, and not for the Commissioner of Internal Revenue, to decide how his operations are to be carried on. In the instant case the petitioner had the primary purpose and intent throughout the tax year of accumulating as large a number of shares of U.G.I. as market conditions would permit. To this end, when he thought conditions favorable he bought. When it turned out that he had made a bad guess as to the course of the market and, consequently, through a fall in daily quotations his account was overloaded and his margin impaired, he intended to sell the certificates, the purchase of which had brought about the condition which made the sale necessary. (*Statement of Evidence*, pars. X, XIV, XIX, R. 44-46).

This evidence, though that of an interested party, being unimpeached and uncontradicted, was binding on the Board and must be regarded as establishing these facts before this Court.

Chesapake & Ohio R. R. Co. v. Martin, 283 U. S. 209, 215, 220.

Chicago Ry. & Equipment Co. v. Blair, 20 Fed. (2d) 10, 12 (C. C. A. 7th).

Under *Mobile, J. & K. R. R. Co. v. Turnipseed*, 219 U. S. 35, if the rule of "first in first out" should be regarded as

merely establishing a "*prima facie* inference", such inference was at an end when petitioner proved his intention corroborated by the detail of the transactions.

That case involved the validity of a provision of the Mississippi Code which provided that (p. 41):

> "In all actions against railroad companies for damages * * * proof of injury inflicted by the runing of the locomotives or cars of such company shall be *prima facie* evidence of the want of reasonable care and skill."

At page 43 the opinion, by Mr. Justice Lurton, reads:

> "The statutory effect of the rule is to provide that evidence of an injury arising from the actual operation of trains shall create an inference of negligence, which is the main fact in issue. The only legal effect of this inference is to cast upon the railroad company the duty of producing *some evidence* to the contrary. *When that is done the inference is at an end* and the question of negligence is one for the jury upon all the evidence."

Under the authority of this case, the Court below erred in holding that the presumption established by the regulation overcame the evidence given by petitioner, which, as noted above, was the only evidence available in the instant case and presumably in any other similar case.

CONCLUSION.

The petition for the writ of certiorari should be granted.

HENRY M. WARD,
Counsel for Petitioner,
Washington, D. C.

January 21, 1935.

APPENDIX A.

Analysis of Schedules (R. 25-28).

An examination of the purchases and sales from month to month, as stated in the Schedules, Exhibits B and C, (R. 25-28) shows that in nearly every instance the most recent purchases tallied with the immediately following sales.

Analysing Exhibit B, the Clothier Jones account, (R. 25-26) it appears that in February (6th and 9th) petitioner sold 400 shares at 113-112 and bought back 400 in March (9-21) at 117-120; that in April he bought 600 between 122 and 134 5/8 and from May 3-7 he bought 600 more shares on a rising scale from 137 to 148 and sold 1,000 shares May 10th at about 145. These sales greatly strengthened his position. On May 14th he bought 500 more at about 148. On the following days the market fell and he was forced to sell 500 shares May 18-23 at a loss of over 5 points. Thus his debit balance by the purchase and sale of these 500 shares was increased by only about $6,000. Thereafter by a fall in the market his margin was impaired, and on June 12, 13 he sold 800 shares on a falling market (139-131¼) but bought back 800 shares on June 15, 19 on a rising market (133 3/8-139). The result of these transactions was almost an even break. His debit on May 31st of $244,035.18 increased to $245,338.16 on June 18. In the meantime his "long" stock had increased by only 200 shares, from 2,300 March 31 to 2,500 June 30th. There were no transactions in July, August or September. On October 8th he bought 500 shares at 140¾ and on October 22nd sold 500 shares between 145½ and 146½, reducing his debit balance of $249,491.38 on September 29 to $246,528.14 on October 31. On November 5th he bought 500 shares at 146½. On November 16th 500 more at 161¼ increasing his debit balance to $403,403.14. On December 10-11 the market being off nearly 10 points, he sold 500 shares at 151-152 1/8. This purchase of 500 shares in November and sale of 500 in

December cost him nearly $10,000. His debit balance of $319,903.14 on November 5th was increased to $329,840.44 on December 11th. December 13-26 he bought 500 more shares at 157¼-162 and made no further purchases or sales. His "long" holdings of 2,500 shares on October 31st, (an increase of only 200 over the 2,300 held on January 1st) were increased by 1000 shares to 3,500 on December 31st, an increase for the year in the Jones account of 1,200 shares.

Similarly, analysing the MacDonald account, Exhibit C (R. 27-28); petitioner started on January 1st "long" 3,000 shares, with a debit balance of $283,168.64. January 16th he bought 100 shares at 116½. February 6th he sold 200 shares at 113 and February 9th 200 at 112, making 400 sold in February; March 9-12 he bought back 400 shares at 115 7/8-120½. The net result to March 31st was an increase from 3,000 to 3,100 shares and an increase of debit balance from $283,168.64, January 1st, to $297,938.74, March 31st. In April, on a rising market, petitioner bought 600 shares at 122½-134. May 3rd-8th he bought 600 more at 137-148. These purchases increased the debit balance from $297,938.74, March 31st, to $460,337.54. Consequently, the margin being impaired, petitioner on May 10th sold 1,000 shares at 144 5/8-144¾ and on May 11th 500 more at 146. As the result of these transactions petitioner's "long" account was reduced from 3,700 shares April 30th to 2,800 shares May 11th and his debit balance was reduced from $374,487.54 to $243,205.04. With his 2,800 shares at the quotation of 146 he had a credit equal to $408,800. The debit of $243,205.04 is 70 per cent of $347,421.48, so petitioner had a surplus credit of over $61,000. Accordingly on May 14 he bought 500 shares at 147¼-147 3/8 and on May 25th 200 shares more making him long 3,500 shares on May 31st with a debit balance of less than 70 per cent of the market quotations. In June, his margin being impaired, he sold 800 shares June 12-13 on

a falling-market (139-131) decreased his holdings to 2,700 shares and his debit balance from $247,968 on May 31st to $240,034 June 13th. These sales brought his debit balance below 70 per cent of the current quotation, so, on June 14-18 he bought back 800 shares on a rising market from 134 5/8 to 139. His holdings were thus restored to 3,500 shares. His debit balance, which had been $347,968 on May 31st was increased to $349,384. On June 21st, the market being off and his margin impaired, he sold 500 shares at 133 and reduced his debit balance to $283,519. On June 29th he bought 200 shares at 135 7/8. As his debit balance was less than 70 per cent of the market quotation he was able to buy 300 shares more July 2-5 at 137-138. This brought his "long" account on July 31st to 3,500 shares and his debit balance to $353,152.96. He did not operate in August, but September 14th sold 1,000 shares at 142¾-143 7/8. This sale reduced his debit balance to $212,766.23 and his long account to 2,500 shares. On October 3d he bought back 1,000 shares at 141, made no further sales, and, in November bought 1,000 more shares on a sharp rise at 156½-168. There were no purchases or sales in December and on December 31st his account stood "long" 4,500 shares, debit balance $525,527.99.

From this analysis on the year's transactions, assuming that the market quotation was 160 on December 31st, 1928

and 115 on January 1st, his accounts with the two brokers stood as follows:

1928 Dec. 31 "long" 8,000 shares at 160 (approximate market quotation).....	$1,280,000.00
Less total debit balances both brokers	932,822.67
"Paper profit" on all transactions 1928 and prior years.....	$347,177.33
Jan. 1 "long" 5,300 shares at 115 (approximate market quotation)	$609,500.00
Less total debit balances both brokers	501,865.59
Paper profit years prior to 1928.....	$107,634.41
Hence the "paper profit" for 1928 was, the total profit to December 31, 1928, as above.....	$347,177.33
less the paper profit as at Jan. 1, 1928, as above.....	107,634.41
Making the "paper profit" for 1928..	$239,542.92

These "paper profits", being mere increments of value in securities held, were of course not taxable. The Commissioner, however, by applying the rule of "first in, first out", computed an *actual profit,* realized by sales, of (R. 22) $192,143.25, only some $47,000 less than the non-taxable "paper profit" for the year. Indeed by taking the market value of shares on hand January 1, 1928, at a few points higher than the assumed 115 and on December 31, a few points lower than the assumed 160, the actual profit for the year determined by the Commissioner would be greater than the non-taxable "paper profit".

APPENDIX B.

SNYDER V. COMMISSIONER, PETITIONER'S RECOMPUTATION OF TAX 1928.

(Illustration only, based on return, not printed, and Exhibits B and C, R. 25-28, and on Appendix A, analysis of transaction above, pages 26-29)

1. Computation of net taxable income.

1	Salary			$5,500.00
2	Commissions, etc.			554.18
3	Profit on sales of stock (a) Clothier Jones account (Exhibit B, R. 25-26) 1928 bought 3700 shares U. G. I. at following prices:			
	Shares 1600 for	$209,975.00		
	Shares 1300 for	183,300.00		
	Shares 800 for	84,775		
	3700 shares bought for	$478,050.00		
	1928 Sold 3700 shares for		$516,313.50	
	Less price paid above		478,050.00	
	Profit on Clothier Jones account			38,263.50
	(b) MacDonald & Co. account (Exhibit C, R. 27-38) 1928 total shares bought 5700 for		806,687.50	
	Less price paid for last 1500 shares, viz:			
	Nov. 2 500 shares	84,125.00		
	Nov. 8 500 shares	78,375.00		
	Oct. 3 500 shares (1½ of 1000)	70,625.00		
	Total deduct for 1500 shares	233,125.00	233,125.00	
	Net paid for 4200 shares		$573,562.50	
	1928 Sold 4200 shares for		$578,991.00	
	Less purchase price as above		573,562.50	
	Profit on MacDonald account			5,428.50
	Add dividends			33,363.55
	Gross income			$83,109.73
	Deduct interest paid brokers			43,427.63
	Net taxable income			$39,682.10

Computation of tax			
Normal tax			
Net taxable income as above	$39,682.10		
Less dividends as above	33,363.55		
Balance subject to normal tax	6,318.55		
Subject to 1½%	4,000.00	60.00	
Balance to 3%	2,318.55	69.56	
Total normal tax			129.56
Surtax			
Net taxable income above	$39,682.10		
Surtax on	36,000.00	1,400.00	
Balance at 10%	3,682.10	368.21	
Total surtax			1,768.21
Total tax 1928			$1,897.77

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. 663.

JOHN A. SNYDER, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

On a Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

REPLY BRIEF FOR PETITIONER.

Petitioner, with respondent's consent, submits the brief filed in support of the petition as petitioner's brief, the necessary changes in the page references to the record having been made.

At page 5 of the Government's brief, in the instant case, its brief in the *Rankin* case, in which its argument is made, is adopted. Similarly, this petitioner adopts the respondent's brief in the *Rankin* case with the reservation that petitioner submits that, in the instant case, petitioner's intention to sell the last acquired stock first is as fully established as in that case.

SUMMARY OF ARGUMENT.

FIRST. THE GOVERNMENT CONCEDES THAT PETITIONER INTENDED TO SELL THE LAST ACQUIRED SHARES FIRST, BUT CONTENDS THAT THIS INTENTION IS IMMATERIAL.

SECOND. PETITIONER'S INTENTION TO SELL THE LAST ACQUIRED SHARES IS SHOWN BY THE RECORD TO HAVE BEEN CARRIED INTO EFFECT.

THIRD. THE RESPONDENT HAS NOT CORRECTLY STATED PETITIONER'S POSITION.

FOURTH. SECTIONS 111, 112 AND 113 OF THE REVENUE ACT OF 1928, ON WHICH RESPONDENT RELIES, ARE INAPPLICABLE TO CURRENT TRANSACTIONS OF PURCHASE AND SALE ON MARGIN DURING THE TAX YEAR SUCH AS HERE INVOLVED.

FIFTH. THE REGULATION INVOLVED IS NOT A RULE OF SUBSTANTIVE LAW, BUT, AT MOST, A MERE *prima facie* PRESUMPTION, OR INFERENCE OF FACT, WHICH BECAUSE OF THE EVIDENCE TO THE CONTRARY, IS AT AN END.

SIXTH. THE REGULATION INVOLVED, IF APPLICABLE, IS CONCEDEDLY IRREBUTTABLE WITH RESPECT TO THE IDENTIFICATION OF SHARES OF STOCK, IN THE FORM OF STREET CERTIFICATES, CARRIED IN A MARGIN ACCOUNT, AND THEREFORE AD HOC BEYOND THE POWER OF THE COMMISSIONER.

SEVENTH. SHOULD IT BE HELD THAT THE REGULATION IS VALID AND ENFORCEABLE WITH RESPECT TO THE TRANSACTIONS HERE INVOLVED AND THAT IT IS NOT AT AN END UPON THE EVIDENCE, IT SHOULD BE LIMITED, IN ITS APPLICATION TO THE PURCHASES IN THE TAX YEAR AND NOT APPLIED TO PURCHASES IN PRIOR YEARS.

FIRST.

THE GOVERNMENT CONCEDES THAT PETITIONER INTENDED TO SELL THE LAST ACQUIRED SHARES FIRST, BUT CONTENDS THAT THIS INTENTION IS IMMATERIAL.

At page 5 of respondent's brief in the instant case it is stated:

> "The taxpayer intended to sell the last shares acquired by him."

At page 12 (Rankin brief) the Government contends:

> "We submit the taxpayer's intention is without bearing on the question here. It is apparent from the language of the regulation that actual identification and not mere intent is the controlling factor."

At page 15 (Ibid.) it is said:

> "Since the broker cannot identify, it is not apparent how the communication of the taxpayer's intention to the broker can add anything to the intention itself."

And at page 28 (Ibid.):

> "The real burden of taxpayer's complaint is not that he has been deprived of an opportunity to make a defense, but rather that he has no defense to offer, which in turn is due, not to the assailed regulation, but to the nature of the transaction in which he voluntarily engaged."

This contention clearly shows that the regulation is arbitrary and oppressive. In the instant case the tax due, by application of the regulation has been increased from $1897.77 (petitioner's brief, p. 30, Appx. B) to $38,961.22. (R. 18.) The net taxable income in the tax year of about $39,682.10, has been increased to $197,495.85. (Ibid.)

SECOND.

PETITIONER'S INTENTION TO SELL THE LAST ACQUIRED SHARES FIRST IS SHOWN BY THE RECORD TO HAVE BEEN CARRIED INTO EFFECT.

It is pointed out in petitioner's brief (p. 24) that in the instant case the only evidence which could be available was introduced, namely; (1) *his intention* (a) to accumulate as many shares of U. G. I. as he could; (b) to sell the shares the purchase of which had, on a fall in daily quotations, impaired his margin; (c) to buy back an equal or greater number of shares, when in his judgment, the market condition was favorable; (2) *the carrying out of this intention by action* as shown by the Statement of Evidence (R. 31-32) the schedules of purchases and sales (R. 18-21) and the analysis of the same (Appendix A, to petitioner's brief, pp. 26-29).

This analysis shows clearly that whenever petitioner sold shares he promptly, within a few days or weeks, bought back an equal or greater number. Thus, between April 2d and 30th, he bought 600 shares in 6 lots of 100 each. May 3d-7th he bought 600 more in 100 share lots. May *10th* he sold 1000 shares at a substantial profit over the purchases in April and May and on May *14th* he bought back 500 shares. May 18-23, on a falling market he *sold 500* shares and June 14-18 *bought back 800* shares on a rising market. (R. 18-19; brief, p. 26) The other transactions were similar (R. 18-21; brief, pp. 26-29).

Thus petitioner's intention to sell was supported by his acts. He *intended* to sell the last acquired shares. He usually *sold* shares within a few days after acquiring them *on a falling market* (R. 18-23 column of quotations "4t" 133 3/8, 139, etc., etc.). In a few instances he realized a "quick profit". (*Analysis*, petrs.' brief, pp. 26, 28; *Schedules*, R. 19, 21, sales in September and October.)

Not only did petitioner prove the sales in 1928 in accordance with his intention, but he alleged and respondent admitted that he had the intention throughout the period from 1924 to 1928 of increasing his long account through the process of "pyramiding". (R. 4-5, petition to B. T. A., pars. V-VII. Admitted, R. 21-22.)

The proof of overt acts coupled with proof of intention not only justifies the inference but *compels the conclusion*, in the absence of evidence to the contrary, *that the sales were made in accordance with the intention.* No sane man, under the circumstances, would do anything else than sell the shares, the purchase of which had brought about (following a fall in daily quotations) the necessity of either putting up more margin or reducing the debit balance to less than 70 per cent of the current daily quotations of the shares held in his long account. (Statement of Evidence R. 32) These incidents are common to all speculative margin accounts when the market is active.

Petitioner, might have increased his collateral or reduced the debit balance by payments of cash. He elected, as he had a perfect right to do, to sell shares, even at a loss, in order to apply the proceeds to the reduction of the debit balance.

The evidence is clear and convincing and, being neither impeached nor contradicted, establishes the facts as matter of law under the authorities cited at page 24 of petitioner's brief.

The Statement of Evidence on this point is as follows:

> (R. 31-32) "It was the intention of the petitioner throughout the year 1928 to increase his holdings of shares of the (U. G. I.) stock in his margin accounts with the stock brokers. In each instance of sale of stock on the dates and in the amounts specified in the schedules (R. 18-21)—the respective stock brokers required the petitioner, because of a fall in the market quotations of said U. G. I. stock, either to put up more margin—or to increase his credit balance by selling a sufficient number of shares of the said stock. In *each of such instances petitioner ordered*

said brokers to sell the various amounts of such stock mentioned in said Exhibits B and C (R. 18-21) at the quotations in force on the day of sale, and *in each instance* petitioner had *the intent and purpose of buying back equal or greater amounts of said stock* shortly thereafter. It was not *at any time* the petitioner's intention to sell *any of the shares of stock purchased in prior years,* which showed a large paper profit, but it was his intention in each instance of sale on the dates and in the amounts specified in said Exhibits B and C to sell the last acquired stock, *the purchase of which • • • had brought about an impairment of his margin* below the 30 per cent margin which the brokers required him to maintain."

"Paragraph XIV. All the transactions in the year 1928 of said brokers in the purchase and sale of U.G.I. stock which had the effect of strengthening petitioner's position in the stock market were made for that purpose. • • •"

"Paragraph XIX • • • Throughout 1928 the petitioner did not intend to make any large profits computed by reference to the purchase price in prior years and the sale price of an equal number of shares in 1928. *Nor, if such profits had been made, could they have been withdrawn in cash without impairing petitioner's margin* and thereby necessitating the sale of additional shares."

This evidence is unimpeached and uncontradicted.

The Court of Appeals appears to have overlooked this evidence. Their opinion reads (R. 40):

"He proved what he had thought and *also proved that he had done nothing about it.*"

As pointed out above the evidence shows without impeachment or contradiction that petitioner every time he ordered his brokers to sell intended to sell the stock the purchase of which had brought about the impairment of his margin. In view of the admission that the brokers were under no obligation to sell any specified certificates or

shares, but customarily sold such street certificates as were most conveniently available (R. 10, pet'n to B. T. A., par. XII; admitted, p. 22) a written order to the brokers to sell from any particular lot would have been an idle ceremony; as would have been any book entry or memorandum or declaration, further evidencing petitioner's intent. Any such evidence would have been merely cumulative of petitioner's proved and conceded intent.

On this point the Government and petitioner are in accord.

Respondent states in his brief, page 6:

> "As pointed out in our brief in the Rankin case, since the broker cannot identify the stock sold, it is not apparent how the communication of the taxpayer's intention to the broker can add anything to the intention itself."

THIRD.

THE RESPONDENT HAS NOT CORRECTLY STATED PETITIONER'S POSITION.

At page 7 of the Government's brief in the *Rankin* case it is stated (referring to Sections 111, 112 and 113 of the Revenue Act of 1928, printed in full below, Appendix B, pp. 26-35):

> "The parties here agree that these statutes are applicable."

See further *Ibid*, pp. 2-3, where these sections are quoted in part.

On the contrary, petitioner contends that the applicable statute is comprised in Sections 11, 12, 21, 22 and 23 of the Act, quoted, so far as relevant, in Appendix A, below p. 24.

Respondent contends (*Rankin* brief, p. 28):

> "And it is because of *the very nature of the transaction which makes identification impossible*, that a rule of this kind becomes necessary. The rule is reasonable under the circumstances. It is certainly *the most convenient* from an administrative standpoint. It oper-

ates to the taxpayer's advantage as much as to his disadvantage. Under it he is taxed only on what is his true income. He can offer no better rule."

The fallacy of these contentions is plain. Petitioner, because in 1928 he *was operating in the same stock* which he had accumulated through similar operations in prior years, is taxed $38,961.22. (R. 18) Had his credit balance—his "long" account—been on January 1, 1928, the same in value but in other securities, his tax, even if the regulation were enforced with respect to his sales in that year, would have been but $1897.77 or thereabouts. (Petrs.' brief, Appx. B,* p. 30)

Upon a rising market the enforcement of the regulation increases the tax in this instance more than twenty fold. It can operate to a taxpayer's advantage only on a falling market with which these cases are not concerned.

Can it properly be said that a taxpayer's "true income" in a given tax year is to be measured, not by the result of his active trading operations for that year, but by going back three (or logically twenty) years to ascertain the cost of stock which the taxpayer in the tax year intended to hold for sale in a subsequent year?

As pointed out in petitioner's brief (p. 19) the "long" account to his credit on January 1, 1928, served merely as collateral to enable him to carry on his extensive trading during the year—purchases of 10,600 shares of U. G. L., in 73 transactions, at a cost of ~~$1,095,304.50~~ 4,637.50, sales of 7900 shares in 50 transactions for $1,095,304.50.

Petitioner has and offers a "better rule," namely, that with respect to trading on active margin accounts the year's operations be computed by taking the difference between the purchase price and the sales price of shares bought and sold during the year, deducting expenses, such as commissions, taxes and interest, (under Section 23) and ascertaining whether the result for the year is a profit or a loss. If

*This computation is made without reference to the regulation and without reference to the disallowance of losses on so-called wash sales (Sec. 118, below p. 35 and Sec. 23(e) p. 24). It is our contention that these provisions are inapplicable. This precise point is not here involved.

the sales exceed the purchases, and are not "short" sales, then ascertain what shares on hand the first of the year, the taxpayer intended to sell. This is the method adopted with respect to dealings in other commodities, except where, under Section 22 (c) the inventory basis is used. As noted below (pp. 22-23) the inventory basis is not, under the regulations, used with respect to operators on margin accounts, who, like the petitioner, are officers of corporations.

This Court has held in *Heiner v. Donnan*, 285 U. S. 312, that the difficulty of enforcing the collection of a tax does not justify a statutory presumption, whether conclusive or irrebuttable.

As said by the Supreme Court of Pennsylvania in *L. H. Taylor & Co.'s Assigned Estate*, 192 Pa. 304:

> "Stocks are as legitimate subjects of speculative buying and selling as dry goods or pig iron. A man may buy any commodity, stock included, to sell on an expected rise."

FOURTH.

SECTIONS 111, 112 AND 113 OF THE REVENUE ACT OF 1928, ON WHICH RESPONDENT RELIES, ARE INAPPLICABLE TO TRANSACTIONS OF PURCHASE AND SALE ON MARGIN DURING THE TAX YEAR SUCH AS HERE INVOLVED.

While true that the short excerpts from Sections 111, 112 and 113, quoted at pages 2-3 of the Government's brief in the Rankin case, afford a plausible contention that those sections relate to current transactions of purchase and sale on margin, "trading on the stock exchange," such as are here presented, analysis of these sections shows that they relate to an entirely different subject matter, namely, the sale of property, including securities, held for investment over a period of years, "capital assets".

This Court has recently, in *Helvering v. New York Trust Co.*, 292 U. S. 455, held that the intent of Congress is not to

be ascertained from isolated phrases or paragraphs of a Revenue Act, but that, not only the context, but the Act as a whole must be considered.

The context clearly shows that Sections 111, 112 and 113 relate solely to the sale of property held for investment,—capital assets.

As pointed out in petitioner's brief, page 17, the primary intent of Congress is to require

> "the computation of gains and losses on the basis of an annual accounting *for the transactions of the year*" (*Woolford Realty Co. v. Rose*, 286 U. S. 319, 326, following *Burnet v. Sanford & Brooks Co.*, 282 U. S. 359, 363).

Sections 111, 112 and 113, must, therefore, be read, as must other detailed provisions, in the light of the controlling provisions of Sections 11, 12, 21, 22 and 23, as construed in the cases last above cited.

It is also to be borne in mind that any doubt as to the construction of the Act is to be resolved in favor of the taxpayer. This point is so well settled that it is not necessary to call attention to any cases in addition to *United States v. Merriam*, 263 U. S. 179.

Sections 11 and 12 provide that normal tax and surtax respectively shall be levied "for each taxable year" equal to the stated percentages of "the net income in excess of credits, etc."; net income is defined by Section 21 as "the gross income computed under Section 22 less the deductions allowed by Section 23. Section 22 defines (by general definition) "gross income" as including "gains, profits and income derived from trades, businesses,—or sales or dealings in property growing out of the use of or interest in such property—or the transaction of any business carried on for profit."

As pointed out in petitioner's brief, pages 16-17, Section 22 is controlled by Section 11 and the phrases "sales or dealings in property" and "transactions entered into for

profit" mean sales *or dealings in property* and transactions, *for each taxable year*. These sections therefore cover the transactions of petitioner and state the basis for computing net taxable income.

With these rules in mind the following analysis of Sections 111, 112 and 113 is submitted. These sections are quoted in full in Appendix B, pages 26-35 below.

Section 111, (a), (b), and (c) (p. 26 below) on which respondent relies, relates to the sale of capital assets or property held for investment, and not to *current purchases and sales* during the tax year of shares of stock or other commodities. Thus subsection (b), (1) and (2), clearly relate to capital assets and authorize the deduction from "the basis provided in section 113" of (1) "any expenditure, receipt, loss or other item, properly chargeable to capital account, (2) that this basis shall be diminished by exhaustion, wear and tear, obsolescence, amortization and depletion which have since the acquisition of the property been allowable under this Act *or prior income tax laws.*" There follows a specific provision that "diminution in respect of depletion" shall not exceed the depletion allowance, under Section 114 (b) (2) for mines discovered *after February 28, 1913*, and, under Section 114 (b) (3), of 27½ per cent of annual gross income derived from oil and gas wells to the extent of 50 per cent of net income.

Obviously, all these extremely detailed provisions relate to physical property, real estate, buildings, machinery, equipment and the like. None of them has any application whatever to marginal transactions in shares of stock.

Coming now to subsection (3) of Section 111 (b) (p. 26 below) we find a specific reference to "stock" which on its face is inapplicable to current transactions of purchase and sale throughout the tax year such as are involved in the instant case.

Subsection (b) (3) reads:

> "*In the case of stock* the basis (as defined in Section 113) shall be diminished by the amount of distributions

previously made in respect of such stock to the extent provided *under the law applicable to the year in which the distribution was made.*"

This specific provision clearly relates only to shares of stock held for investment, or as a capital asset, over a period of years. It has no application on its face to an active trading account on margin with current purchases and sales in the tax year, such as is presented in the instant case.

Reference to the "basis provided in section 113" fortifies and establishes this conclusion.

Section 113 (a) (p. 30 below) reads:

"BASIS FOR DETERMINING GAIN OR LOSS.

"(a) *Property acquired after February 28, 1913*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property."

While, taken literally, (as by the respondent, brief, pp. 2-3; 7-8) this provision might be held applicable to trading on margin and to cover the sales involved in the instant case, the context and the minute and detailed provisions in the twelve numbered paragraphs of subsection (a) clearly show that Congres had in mind (with respect to stock) only shares of stock held for investment—capital assets. There are detailed provisions (pp. 31-35 below) for (1) "INVENTORY VALUE"; (2) "GIFT AFTER DECEMBER 31, 1920"; (3) "TRANSFER IN TRUST AFTER DECEMBER 31, 1920"; (4) "GIFT OR TRANSFER IN TRUST BEFORE JANUARY 1, 1921"; (5) "PROPERTY TRANSMITTED AT DEATH"; (6) "TAX FREE EXCHANGES GENERALLY" (under Section 112); (7) "TRANSFER TO CORPORATION WHERE CONTROL OF PROPERTY REMAINS IN SAME PERSONS": (8) "CORPORATION CONTROLLED BY TRANSFEROR"; (9) "TAX FREE DISTRIBUTIONS" (distributed after December 31, *1923* under Section 112); (10) "INVOLUNTARY CONVERSION" (under Section 112); (11) "WASH SALES OF STOCK";* (12) "PROPERTY ACQUIRED DURING AFFILIATION".

*Sold in prior years, p. 34, *infra*.

Subsection (b) specifically relates to "*Property acquired before March 1, 1913.*"

Section 112 (pp. 27-30 below) provides similarly in great detail for "RECOGNITION OF GAIN OR LOSS." It first lays down a "GENERAL RULE" as follows:

> (a) "Upon the sale or exchange of property the entire amount of the gain or loss, determined under Section 111, shall be recognized, *except as hereinafter provided in this section.*"
>
> "Subsection (b) *Exchanges solely in kind*
>
> (1) PROPERTY HELD FOR PRODUCTIVE USE OR INVESTMENT—No gain or loss shall be recognized if property held for productive use in trade or business or for investment (not including stock in trade or other property held primarily for sale, nor stocks, bonds, notes, choses in action, certificates of trust or beneficial interest, or other securities or evidences of indebtedness or interest) is exchanged solely for property of a like kind to be held either for productive use in trade or business or for investment,"

Note that the specific reference to "stocks" in this subsection is controlled by the generic sub-title, "Property held for productive use or investment." Hence shares carried on an active margin trading account are not affected.

Then follow detailed provisions under various headings (pp. 27-30 below) numbered from (b) (2) to (b) (5) all clearly relating to capital assets; paragraphs under subsection (c) (1) and (2) "Gain from exchanges not solely in kind," which qualify subsection (b); two paragraphs under subsection (d) "Same—gain of corporation"; (e) "Loss from exchanges not solely in kind," (f) "Involuntary conversions," (g) "Distribution of stock on reorganization," (h) "Same—effect on future distribution," (i) (1) and (2) "Definition of reorganization"; (j) "Definition of control."

Under settled rules of statutory construction these extremely detailed and minute provisions with respect to profit or loss upon the sale or conversion of investment property or capital assets, especially when read in the light of Section 101, relating to "Capital Net Gains and Losses," (giving the taxpayer the option of a special rate of 12½ per cent on gains derived from the sale of "capital assets" held for more than two years) exclude the hypothesis that in enacting those provisions Congress had in mind the sale of shares of stock held in active margin accounts and bought solely (as in the instant case) for trading, as distinguished from investment.

Indeed the Commissioner when he promulgated Article 58 ("first in first out") made it in enlargement or explanation, not of these Sections (111-113) but of Section 22, the definition of "gross income." Articles 561-604, forty-four articles of Regulation 74, relate specifically to Sections 111-113.

It follows that Sections 111-113 are inapplicable to the transactions involved in the instant case, and do not authorize the regulation, here involved, to be applied to the transactions of the petitioner.

FIFTH.

THE REGULATION INVOLVED IS NOT A RULE OF SUBSTANTIVE LAW, BUT, AT MOST, A MERE PRIMA FACIE PRESUMPTION, OR INFERENCE OF FACT, WHICH, BECAUSE OF THE EVIDENCE TO THE CONTRARY, IS AT AN END.

It is idle for respondent to contend (Rankin brief, pp. 23-24) that "the rule here is not so much a rule of evidence as a rule of substantive law." The same contention, with far stronger grounds on which to base it, was made in *Heiner v. Donnan*, 285 U. S. 312. On this point the opinion reads (pp. 328-329):

> "The government makes the point that the conclusive presumption created by the statute is a rule of

substantive law, and regarded as such should be upheld; and decisions tending to supplant that view are cited. The earlier revenue acts created a *prima facie* presumption, which was made irrebuttable by the later act of 1926. *A rebuttable presumption clearly is a rule of evidence* which has the effect of shifting the burden of proof, *Mobile, J. & K. R. Co. v. Turnipseed*, 219 U. S. 35, 43; and it is hard to see how a statutory rebuttable presumption is *turned from a rule of evidence into a rule of substantive law* as the result of a later statute making it conclusive."

The Court then cites *Schlesinger v. Wisconsin*, 270 U. S. 230; *Bailey v. Alabama*, 219 U. S. 219, 238, and *Manley v. Georgia*, 279 U. S. 1, 5-6, from which last case an excerpt is quoted, and continues (p. 329):

> "If a legislative body is without power to enact as a rule of evidence a statute denying a litigant the right to prove the facts of his case, certainly the power cannot be made to emerge by putting the enactment in the guise of a rule of substantive law."

See further to same effect *United States v. Provident Trust Co.*, 191 U. S. 272, 283.

Respondent takes two inconsistent positions.

First (p. 22, Rankin brief):

> "But in marginal transactions, particularly in pyramiding operations such as those in the Snyder case, it is *impossible* for the taxpayer to identify. In such cases the need for such a rule as this seems apparent."

Upon this premise respondent bases the wholly unwarranted conclusion, directly contrary to the considered opinion of this Court in *Heiner v. Donnan*, that the regulation is valid as a rule of substantive law (Ibid, p. 23) analogous to the *conclusive presumptions of law* with regard to the age of an infant, etc., etc. (Ibid pp. 24-25).

Second (Ibid p. 27):

> "The taxpayer is given *every opportunity to identify the shares he has sold* and to prove his gain or loss accordingly. The regulation does not deny the taxpayer a fair opportunity to offer testimony as in *Bailey v. Alabama, supra,* and *Manley v. Georgia, supra.*"

Respondent then quotes an excerpt from *Mobile etc. R. R. v. Turnipseed,* 219 U. S. 35, 43 (included in the quotation from *Bailey v. Alabama,* 219 U. S. 219, 238, at page 23 of petitioner's brief), but fails to quote the preceding portion of the opinion quoted in full in petitioner's brief, page 25, that when "some evidence to the contrary" of the inference of fact raised by the presumption is introduced, "the inference is at an end."

In respondent's brief, pp. 24, 25, there are references to Chamberlayne on Evidence and Wigmore on Evidence. All of the "conclusive presumptions" there referred to are not presumptions, or statutory inferences, of fact but presumptions of law. In other words, they are provisions of substantive law and not rules of evidence. Under this classification are included the rules with regard to the age of a child at which a criminal intent can be formed, the age at which certain crimes may be committed and consent given. So, with regard to the effect of tax deeds, deeds registered a certain number of years, the citizenship of stockholders of a corporation. The statutory imposition of liability on cities for damages by mob violence is, of course, not a rule of evidence at all.

Atlantic Coast Line v. Riverside Mills, 219 U. S. 186, cited at page 24, does not relate to an inference of fact, but to a rule of substantive law, namely, that the initial carrier should be liable for loss or damage to goods shipped on a through bill of lading over the lines of connecting carriers. The statute (Carmack Amendment) was sustained

on the theory that it made the initial carrier the principal contractor, and the connecting carriers its agents (p. 206). There was no question raised as to presumptions of law or of fact. The only question was as to the power of Congress to prohibit the initial carrier from limiting its contractual liability to carriage over its own lines.

The statutory presumption that dividends are presumed to have been paid out of past accumulated profits or surplus, is a rule of substantive law, enacted in order to avoid the question of constitutionality which would arise with regard to the power of Congress to tax dividends paid out of surplus accumulated prior to the adoption of the Sixteenth Amendment. See *Helvering v. Canfield*, 291 U. S. 163, p. 19 below.

The regulation clearly raises an inference of fact and nothing more. It reads:

> "When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots cannot be determined"

That is to say cannot be proved *by evidence*,

> "the stock sold shall be charged against the earliest purchases of said stock."

In other words when the taxpayer fails to show by some form of identification which shares are sold *the fact* is presumed, or inferred, that the shares sold are those earliest purchased.

This Court has held in *Mobile etc. R. R. v. Turnipseed*, 219 U. S. 35, that when evidence to the contrary of such an inference is introduced "the inference is at an end" (quoted Petrs. brief, p. 25).

Respondent cites, as noted above, 5 Wigmore on Evidence 2d Ed. Sec. 2492 (brief pp. 23-24), upon the entirely unsound contention that the regulation establishes a *conclusive presumption of law* or a rule of substantive law.

That author states at the immediately preceding section, 2491 (Vol. 5, p. 452) the rule with regard to presumptions or inferences of fact, substantially as in the cited excerpt from the *Mobile-Turnipseed* case, as follows:

> "It is therefore *a fallacy* to attribute • • • an artificial probative force to a presumption, *increasing* for the jury *the weight of the facts,* even when the opponent has come forward with *some* evidence to the contrary. For example, if death be the issue, and the fact of absence for seven years unheard of be conceded, but the opponent offers evidence that the absentee, before leaving, *proclaimed his intention* of staying away for ten years, until a prosecution for crime was barred, this satisfies the opponent's duty of producing evidence, *removing the rule of law;* and, when the case goes to the jury, they are at liberty to give *any probative force they think fit* to the fact of absence for seven years unheard from. *It is not weighed down with any artificial additional probative effect.* • • •"

See also to same effect, Jones on Evidence in Civil Cases, 3rd Ed. Sec. 104.

See also *Sweeney v. Erving,* 228 U. S. 233, 240, 241, *res ipsa loquitur* rule.

It follows that, assuming that the regulation is applicable to the instant case, it raises a mere inference of fact. Evidence to the contrary having been introduced, the inference is at an end. This evidence being unimpeached and uncontradicted the fact is established that the last acquired stock was sold in each instance. Hence the tax should be recomputed and the court below erred in sustaining the Board of Tax Appeals.

SIXTH,

THE REGULATION INVOLVED, IF APPLICABLE, IS CONCEDEDLY IRREBUTTABLE, WITH RESPECT TO THE IDENTIFICATION OF SHARES OF STOCK, IN THE FORM OF STREET CERTIFICATES CARRIED IN A MARGIN ACCOUNT, AND THEREFORE AD HOC BEYOND THE POWER OF THE COMMISSIONER.

Respondent contends (Rankin brief, pp. 23-26), that the regulation is conclusive, in other words irrebuttable. This point is discussed fully in petitioner's brief, pages 21-23. We shall confine ourselves in this reply brief to a discussion of certain of the cases cited by respondent (Ibid), namely, those decided by this Court. The other cases cited are either of the Circuit Courts of Appeals or of State courts. Except for *Howbert v. Penrose*, 38 Fed. 2d 577, 578, cited under petitioner's Sixth Point (brief pp. 23-24), which is directly in petitioner's favor, they differ so greatly on the facts, as not to require detailed discussion.

Burnet v. Houston, 283 U. S. 223, is not in point. The question was as to value of property acquired before March 1, 1913, sold at a loss thereafter. The taxpayer did not attempt to prove value on March 1, 1913, so the deduction of the loss was not allowed.

In *Reaves v. Ainsworth*, 219 U. S. 296, 304, the only question involved was as to whether the decision of a military tribunal constituted due process of law. No presumption was involved.

In *Hagar v. Reclamation District*, 111 U. S. 701, 708, the only question involved was as to whether a State statute complied with the due process clause of the Fourteenth Amendment by granting a hearing with respect to an assessment upon land within a reclamation district. No presumption was involved.

In *Helvering v. Canfield*, 291 U. S. 163, the statute (Revenue Act 1921, par. 201, 42 Stat. 228) provided that distributions to stockholders out of accumulated earnings and profits should be (for the purposes of the Act) out of

profits accumulated after February 28, 1913, and should be taxable, but that distributions from profits, etc., accumulated prior to that date should be exempt. *The only question involved* was as to whether losses in 1915, 1916, should be deducted from the surplus of February 28, 1913, or from subsequent profits. It was held that they should be deducted from the surplus of February 28, 1913.

The statute requiring the distributions to be deemed to have been made out of the later profits was a rule of substantive law. No question of the constitutional validity of any presumption or rule of evidence was involved.

In *Mason v. Routzahn*, 275 U. S. 175, the statute (Revenue Act of October 3, 1917, C. 63 Title XII, 40 Stat. 300, 338), provided that any distribution to stockholders in 1917 or later years should be deemed to have been made from the most recently accumulated undivided profits and taxed at the rate in force *in the year when accumulated*. Mason, a shareholder in the Goodrich company, received five dividends in 1917, all of which were paid out of profits accumulated in 1916. Two of these dividends were declared in 1916. At the time the three others were declared in 1917 there were no net profits for that year, applicable to payment of dividends. It was held, sustaining the District Court, and reversing the Circuit Court of Appeals, that all five dividends were taxable at the 1916 rate. No constitutional question was involved.

Orient Insurance Co. v. Daggs, 172 U. S. 557, 566, turns on the power of a State to prescribe the terms of fire insurance policies. The theory that the statute established a conclusive, or any presumption was rejected (p. 566).

In *MacLaughlin v. Alliance Insurance Co.*, 286 U. S. 244 (cited in respondent's brief in this case p. 9), the question presented related to the gain realized on the sale, in 1928, of securities held *as an investment* for upwards of fifteen years. The rule of "first in first out" was not in anyway involved or discussed.

The two following cases cited by the respondent state clearly the relations between stock brokers and their customers.

In *Gorman v. Littlefield,* 229 U. S. 19, 24, the statement of the relations between stockbrokers and their customers is quoted from *Saxton v. Kessler,* 225 U. S. 90, substantially as stated in the petition in the instant case and admitted (R. 5-11, 21-22) and the opinion continues (p. 24):

> "It is therefore unnecessary for a customer, where shares of stock of the same kind are in the hands of a broker, being held to satisfy his claims, to be able to put his finger upon the identical certificates of stock purchased for him. It is enough that the broker has shares of the same kind which *are legally subject to the demand of the customer* (p. 25) * * *. It was, as we have seen, the duty of the broker, if he sold the shares specifically purchased for the appellant, to buy others of like kind and to keep on hand, subject to the order of the customer, certificates sufficient for the legitimate demands upon him. If he did this, the identification of particular certificates is unimportant."

On this point see the admitted allegations in the petition to the Board of Tax Appeals (R. 11, par. XIII).

In *Duel v. Hollins,* 241 U. S. 523, 529, it was held, following *Gorman v. Littlefield,* that where certificates of a certain stock were found in the box of a bankrupt broker, but for a less number of shares than had been bought for the account of a number of customers, the shares so found should be divided pro rata.

It follows that the cases cited by the respondent do not sustain the Government's contention.

SEVENTH.

SHOULD IT BE HELD THAT THE REGULATION IS VALID AND ENFORCEABLE WITH RESPECT TO TRANSACTIONS OF PURCHASE AND SALE ON MARGIN, IT SHOULD BE LIMITED IN ITS APPLICATION TO THE INSTANT CASE, TO THE PURCHASES IN THE TAX YEAR AND NOT APPLIED TO PURCHASES IN PRIOR YEARS.

If this Court should sustain the regulation against the evidence and further sustain petitioner's contention that (as the purchases exceeded the sales in the tax year), the transactions in 1928 should be segregated and used as the basis for computation, without regard to purchases in prior years, the tax might be increased beyond that computed in Appendix B to petitioner's brief, page 30, but would be far less than the tax assessed* (R. 18).

The purchases on hand exceeded the sales throughout the year, except for the sale of 700 shares in February, bought back in March (*Schedules*, R. 18, 20).

The great difficulty of computing the taxable income without the regulation, on which respondent lays such stress (p. 28) does not exist in the instant case and no reason is perceived justifying the conclusion that in similar cases of marginal trading there should be any serious difficulty if the regulation is held inapplicable.

The basis of computation by inventories (Sec. 22 (c)) is inadmissible. The Commissioner, by Article 105 of Regulations 74, expressly eliminated:

> "Taxpayers *who buy and sell* or hold *securities for* investment or *speculation* and not in the course of an established business and officers of corporations (such as petitioner R. 21, par. V) who in their individual capacities buy and sell securities"

from the class of dealers in securities who may make their returns on the inventory basis.

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*See footnote, p. 8 *supra*.

CONCLUSION.

The judgment below should be reversed and the cause remanded with instructions to recompute the tax in accordance with the views above expressed.

March 11, 1935.

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APPENDIX A

REVENUE ACT OF 1928, SECTIONS 11, 12, 21, 22, 23, AS FAR AS RELEVANT (43 Stat. 791, 795 etc. C. 852)

"Sec. 11. NORMAL TAX ON INDIVIDUALS. (45 Stat. 795) There shall be levied, collected and paid *for each taxable year* a normal tax equal to the sum of the following:

"(a) 1½ per centum of the first $4,000 of the amount of the net income in excess of the credits against net income provided in section 25," etc., etc.

"Sec. 12. SURTAX ON INDIVIDUALS. (Ibid, 796) (a) *Rates of surtax*—There shall be levied, collected, and paid *for each taxable year upon the net income* of every individual a surtax as follows:" etc., etc.

"Sec. 21 (Ibid, 797) NET INCOME.

"Net income 'means the gross income computed under Section 22, *less the deductions allowed by Section 23.*'

"Sec. 22. (Ibid) GROSS INCOME.

"(a) *General definition.* 'Gross income' includes gains, profits and income derived from * * * trades, businesses, * * * or sales, or dealings in property whether real or personal * * * growing out of the ownership or use of or interest in such property; * * * or *the transaction of any business carried on for gain or profit* or gains or profits and income derived from any source whatever.

"Sec. 23. DEDUCTIONS FROM GROSS INCOME. (Ibid, 799) In computing net income there shall be allowed as deductions:

"(a) *Expenses.*—All the ordinary and necessary expenses paid or incurred *during the taxable year* in carrying on any trade or business. * * *

"(b) *Interest*—All interest paid or accrued *within the taxable year* on indebtedness. * * *

"(c) *Taxes generally*—Taxes paid or accrued *within the taxable year.*

"(e) *Losses by Individuals.* In the case of an individual, *losses, sustained during the taxable year* and not compensated for by insurance or otherwise.

"(1) if incurred in trade or business; or

"(2) if incurred *in any transaction entered into for profit,* though not connected with any trade or business."

"(g) *Basis for determining loss*—The basis *for determining the amount of deduction for losses* sustained, to be allowed under *subsection* (e) or (f),* shall be the same as is provided by section 113 *for determining the gain or loss* from the sale or other disposition of property.

"(h) *Loss on sale of stock or securities*—For disallowance of loss deduction in the case of sales of stock or securities where within thirty days before or after the date of the sale the taxpayer has acquired substantially identical property, see Section 118."

Note. While it is provided that *losses,* generally, shall be determined on the basis stated in Section 113 and reference is made with respect to "loss on sale of stock", in Section 118, there is no provision that *profits* or gains shall be computed under these sections.

*Subsection (f) relates to corporations only.

APPENDIX B.

REVENUE ACT OF 1928, C. 852, 45 Stat. 791, 815, 818.

SUPPLEMENT B—COMPUTATION OF NET INCOME.
[Supplementary to Subtitle B, Part II]

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.

(b) *Adjustment of basis.*—In computing the amount of gain or loss under subsection (a)—

(1) Proper adjustment shall be made for any expenditure, receipt, loss, or other item, properly chargeable to capital account, and

(2) The basis shall be diminished by the amount of the deductions for exhaustion, wear and tear, obsolescence, amortization, and depletion which have since the acquisition of the property been allowable in respect of such property under this Act or prior income tax laws; but in no case shall the amount of the diminution in respect of depletion exceed a depletion deduction computed without reference to discovery value under section 114 (b) (2) or to percentage depletion under section 114 (b) (3). In addition, if the property was acquired before March 1, 1913, the basis (if other than the fair market value as of March 1, 1913) shall be diminished in the amount of exhaustion, wear and tear, obsolescence, and depletion actually sustained before such date, and

(3) In the case of stock the basis shall be diminished by the amount of distributions previously made in respect of such stock, to the extent provided under the law applicable to the year in which the distribution was made.

(c) *Amount realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

(d) *Recognition of gain or loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

(e) *Installment sales.*—Nothing in this section shall be construed to prevent (in the case of property sold under contract providing for payment in installments) the taxation of that portion of any installment payment representing gain or profit in the year in which such payment is received.

Sec. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(b) *Exchanges solely in kind.*—

(1) PROPERTY HELD FOR PRODUCTIVE USE OR INVESTMENT.—No gain or loss shall be recognized if property held for productive use in trade or business or for investment (not including stock in trade or other property held primarily for sale, nor stocks, bonds, notes, choses in action, certificates of trust or beneficial interest, or other securities or evidences of indebtedness or interest) is exchanged solely for property of a like kind to be held either for productive use in trade or business or for investment.

(2) STOCK FOR STOCK OF SAME CORPORATION.—No gain or loss shall be recognized if common stock in a corporation is exchanged solely for common stock in the same corporation, or if preferred stock in a corporation is exchanged solely for preferred stock in the same corporation.

(3) STOCK FOR STOCK ON REORGANIZATION.—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

(4) SAME—GAIN OF CORPORATION.—No gain or loss shall be recognized if a corporation a party to a re-

organization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization.

(5) TRANSFER TO CORPORATION CONTROLLED BY TRANSFEROR.—No gain or loss shall be recognized if property is transferred to a corporation by one or more persons solely in exchange for stock or securities in such corporation, and immediately after the exchange such person or persons are in control of the corporation; but in the case of an exchange by two or more persons this paragraph shall apply only if the amount of the stock and securities received by each is substantially in proportion to his interest in the property prior to the exchange.

(c) *Gain from exchanges not solely in kind.*—

(1) If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5) of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

(2) If a distribution made in pursuance of a plan of reorganization is within the provisions of paragraph (1) of this subsection but has the effect of the distribution of a taxable dividend, then there shall be taxed as a dividend to each distributee such an amount of the gain recognized under paragraph (1) as is not in excess of his ratable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913. The remainder, if any, of the gain recognized under paragraph (1) shall be taxed as a gain from the exchange of property.

(d) *Same—gain of corporation.*—If an exchange would be within the provisions of subsection (b) (4) of this section if it were not for the fact that the property received in exchange consists not only of stock or securities permitted by such paragraph to be received without the recognition of gain, but also of other property or money then—

(1) If the corporation receiving such other property or money distributes it in pursuance of the plan of reorganization, no gain to the corporation shall be recognized from the exchange, but

(2) If the corporation receiving such other property or money does not distribute it in pursuance of the plan of reorganization, the gain, if any, to the corporation shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property so received, which is not so distributed.

(e) *Loss from exchanges not solely in kind.*—If an exchange would be within the provisions of subsection (b) (1) to (5), inclusive, of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain or loss, but also of other property or money, then no loss from the exchange shall be recognized.

(f) *Involuntary conversions.*—If property (as a result of its destruction in whole or in part, theft or seizure, or an exercise of the power of requisition or condemnation, or the threat or imminence thereof) is compulsorily or involuntarily converted into property similar or related in service or use to the property so converted, or into money which is forthwith in good faith, under regulations prescribed by the Commissioner with the approval of the Secretary, expended in the acquisition of other property similar or related in service or use to the property so converted, or in the acquisition of control of a corporation owning such other property, or in the establishment of a replacement fund, no gain or loss shall be recognized. If any part of the money is not so expended, the gain, if any, shall be recognized, but in an amount not in excess of the money which is not so expended.

(g) *Distribution of stock on reorganization.*—If there is distributed, in pursuance of a plan of reorganization, to a shareholder in a corporation a party to the reorganization, stock or securities in such corporation or in another corpration a party to the reorganization, without the surrender by such shareholder of stock or securities in such a corporation, no gain to the distributee from the receipt of such stock or securities shall be recognized.

(h) *Same—effect on future distributions.*—The distribution, in pursuance of a plan of reorganization, by or on behalf of a corporation a party to the reorganization, of its stock or securities or stock or securities in a corporation a party to the reorganization, shall not be considered a distribution of earnings or profits within the meaning of section 115 (b) for the purpose of determining the taxability of subsequent distributions by the corporation.

(i) *Definition of reorganization.*—As used in this section and sections 113 and 115—

(1) The term "reorganization" means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected.

(2) The term "a party to a reorganization" includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation.

(j) *Definition of control.*—As used in this section the term "control" means the ownership of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of the corporation.

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that—

(1) INVENTORY VALUE.—If the property should have been included in the last inventory, the basis shall be the last inventory value thereof;

(2) GIFT AFTER DECEMBER 31, 1920.—If the property was acquired by gift after December 31, 1920, the basis shall be the same as it would be in the hands of the donor or the last preceding owner by whom it was not acquired by gift. If the facts necessary to determine such basis are unknown to the donee, the Commissioner shall, if possible, obtain such facts from such donor or last preceding owner, or any other person cognizant thereof. If the Commissioner finds it impossible to obtain such facts, the basis shall be the fair market value of such property as found by the Commissioner as of the date or approximate date at which, according to the best information that the Commissioner is able to obtain, such property was acquired by such donor or last preceding owner;

(3) TRANSFER IN TRUST AFTER DECEMBER 31, 1920.—If the property was acquired after December 31, 1920, by a transfer in trust (other than by a transfer in trust by a bequest or devise) the basis shall be the same as it would be in the hands of the grantor, increased in the amount of gain or decreased in the amount of loss recognized to the grantor upon such transfer under the law applicable to the year in which the transfer was made;

(4) GIFT OR TRANSFER IN TRUST BEFORE JANUARY 1, 1921.—If the property was acquired by gift or transfer in trust on or before December 31, 1920, the basis shall be the fair market value of such property at the time of such acquisition. The provisions of this paragraph shall apply to the acquisition of such property interests as are specified in section 402 (e) of the Revenue Act of 1921, or in section 302 (f) of the Revenue Act of 1924 or the Revenue Act of 1926 (relating to property passing under the power of appointment) regardless of the time of acquisition;

(5) PROPERTY TRANSMITTED AT DEATH.—If personal property was acquired by specific bequest, or if real property was acquired by general or specific devise or by intestacy, the basis shall be the fair market value of the property at the time of the death of the de-

cedent. If the property was acquired by the decedent's estate from the decedent, the basis in the hands of the estate shall be the fair market value of the property at the time of the death of the decedent. In all other cases if the property was acquired either by will or by intestacy, the basis shall be the fair market value of the property at the time of the distribution to the taxpayer. In the case of property transferred in trust to pay the income for life to or upon the order or direction of the grantor, with the right reserved to the grantor at all times prior to his death to revoke the trust, the basis of such property in the hands of the persons entitled under the terms of the trust instrument to the property after the grantor's death shall, after such death, be the same as if the trust instrument had been a will executed on the day of the grantor's death;

(6) TAX-FREE EXCHANGES GENERALLY.—If the property was acquired upon an exchange described in section 112(b) to (e), inclusive, the basis shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the taxpayer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. If the property so acquired consisted in part of the type of property permitted by section 112(b) to be received without the recognition of gain or loss, and in part of other property, the basis provided in this paragraph shall be allocated between the properties (other than money) received, and for the purpose of the allocation there shall be assigned to such other property an amount equivalent to its fair market value at the date of the exchange. This paragraph shall not apply to property acquired by a corporation by the issuance of its stock or securities as the consideration in whole or in part for the transfer of the property to it;

(7) TRANSFERS TO CORPORATION WHERE CONTROL OF PROPERTY REMAINS IN SAME PERSONS.—If the property was acquired after December 31, 1917, by a corporation in connection with a reorganization, and immediately after the transfer an interest or control in such prop-

erty of 80 per centum or more remained in the same persons or any of them, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made. This paragraph shall not apply if the property acquired consists of stock or securities in a corporation a party to the reorganization, unless acquired by the issuance of stock or securities of the transferee as the consideration in whole or in part for the transfer;

(8) SAME—CORPORATION CONTROLLED BY TRANSFEROR.—If the property was acquired after December 31, 1920, by a corporation by the issuance of its stock or securities in connection with a transaction described in section 112(b)(5) (including, also, cases where part of the consideration for the transfer of such property to the corporation was property or money, in addition to such stock or securities), then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made;

(9) TAX-FREE DISTRIBUTIONS.—If the property consists of stock or securities distributed after December 31, 1923, to a taxpayer in connection with a transaction described in section 112(g), the basis in the case of the stock in respect of which the distribution was made shall be apportioned, under rules and regulations prescribed by the Commissioner with the approval of the Secretary, between such stock and the stock or securities distributed;

(10) INVOLUNTARY CONVERSION.—If the property was acquired as the result of a compulsory or involuntary conversion described in section 112(f), the basis shall be the same as in the case of the property so converted, decreased in the amount of any money received by the taxpayer which was not expended in accordance with the provisions of law (applicable to the year in which such conversion was made) determining the taxable

status of the gain or loss upon such conversion, and increased in the amount of gain or decreased in the amount of loss to the taxpayer recognized upon such conversion under the law applicable to the year in which such conversion was made;

(11) WASH SALES OF STOCK.—If substantially identical property was acquired after December 31, 1920, in place of stock or securities which were sold or disposed of and in respect of which loss was not allowed as a deduction under section 118 of this Act, or under section 214(a)(5) or 234(a)(4) of the Revenue Act of 1921, the Revenue Act of 1924, or the Revenue Act of 1926, the basis in the case of the property so acquired shall be the basis in the case of the stock or securities so sold or disposed of, except that if the repurchase price was in excess of the sale price such basis shall be increased in the amount of the difference, or if the repurchase price was less than the sale price such basis shall be decreased in the amount of the difference;

(12) PROPERTY ACQUIRED DURING AFFILIATION.—In the case of property acquired by a corporation, during a period of affiliation, from a corporation with which it was affiliated, the basis of such property, after such period of affiliation, shall be determined, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, without regard to intercompany transactions in respect of which gain or loss was not recognized. For the purposes of this paragraph, the term "period of affiliation" means the period during which such corporations were affiliated (determined in accordance with the law applicable thereto) but does not include any taxable year beginning on or after January 1, 1922, unless a consolidated return was made, nor any taxable year after the taxable year 1928. The basis in case of property acquired by a corporation during any period, in the taxable year 1929 or an subsequent taxable year, in respect of which a consolidated return is made by such corporation under section 141 of this Act, shall be determined in accordance with regulations prescribed under section 141 (b).

(b) *Property acquired before March* 1, 1913.—The basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913, shall be:

(1) the cost of such property (or, in the case of such property as is described in subsection (a)(1), (4), (5), or (12) of this section, the basis as therein provided), or

(2)the fair market value of such property as of March 1, 1913,

whichever is greater. In determining the fair market value of stock in a corporation as of March 1, 1913, due regard shall be given to the fair market value of the assets of the corporation as of that date.

SEC. 118. LOSS ON SALE OF STOCK OR SECURITIES.

In the case of any loss claimed to have been sustained in any sale or other disposition of shares of stock or securities where it appears that within thirty days before or after the date of such sale or other disposition the taxpayer has acquired (otherwise than by bequest or inheritance) or has entered into a contract or option to acquire substantially identical property, and the property so acquired is held by the taxpayer for any period after such sale or other disposition, no deduction for the loss shall be allowed under section 23(e)(2) of this title; nor shall such deduction be allowed under section 23(f) unless the claim is made by a corporation, a dealer in stocks or securities, and with respect to a transaction made in the ordinary course of its business. If such acquisition or the contract or option to acquire is to the extent of part only of substantially identical property, then only a proportionate part of the loss shall be disallowed.

In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 663

JOHN A. SNYDER, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

MEMORANDUM FOR THE RESPONDENT

We do not oppose the granting of a writ of certiorari in this case.

Article 58 of Regulations 74 provides that when shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots cannot be determined, the gain or loss on such sale shall be computed by charging the stock sold against the earliest purchases of such stock.

The petitioner in this case during 1928 and prior years purchased stock through a broker on mar-

gin. In 1928 he sold through the broker a part of such stock. In computing the petitioner's gain on such sale, the Commissioner held that the marginal sales were not identifiable. He accordingly applied the above regulation and matched the sales against the earliest purchases of stock.

The petitioner intended to sell the shares last acquired by him, and the principal question is whether this intention was a sufficient identification of the stock sold so as to take this case out of the regulation. The petitioner also contends that the regulation, if applicable, is unconstitutional. The Circuit Court of Appeals upheld the regulation and held further that mere intention to sell the latest acquired stock was not an identification of the stock sold.

We believe the conclusion reached by the court is right, but feel that much of the court's reasoning is erroneous, particularly when the court attempts to distinguish between shares of stock and certificates of stock, holding that the former are capable of identification even though the identity of the latter be lost.

The case here is practically identical with the case of *Guy T. Helvering, Commissioner of Internal Revenue,* v. *James L. Rankin, Executor of the Estate of Richard B. Turner, deceased,* now pending on the Government's petition for certiorari, No. 582, present term. The *Rankin case* and the

instant case were both decided by the court below on the same day, and in the one opinion the court incorporated by reference much of its reasoning contained in the other (73 F. (2d) 5, 9). The only difference between the two cases is that in the *Rankin case* the taxpayer communicated his intention to dispose of his latest acquired stock to his broker, whereas in this case no such communication was made. The court gave effect to this difference, holding in the *Rankin case* that such communication amounted to identification, but holding in the instant case that the uncommunicated intention did not constitute identification. We submit the distinction made by the court is unsound and that the two cases should have been decided alike (see the *Rankin* petition, pp. 8–9).

The petitioner in the instant case raises several issues which are not present in the *Rankin case*. We feel there is no merit whatever to these contentions. But basically both cases involve the validity of the regulations and its application to substantially the same facts. Because of the similarity in the cases, and because of the general importance of these questions, we do not feel warranted in opposing the present petition.

Should the Court deny the Government's petition in the *Rankin* case, the petition should be denied in this case. If both petitions are granted,

we respectfully suggest that both cases be set for hearing on the same day.

Respectfully submitted.

J. CRAWFORD BIGGS,
Solicitor General.
FRANK J. WIDEMAN,
Assistant Attorney General.
JAMES W. MORRIS,
J. P. JACKSON,
Special Assistants to the Attorney General.

JANUARY 1935.

U. S. GOVERNMENT PRINTING OFFICE: 1935

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In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 663

JOHN A. SNYDER, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The findings of fact and opinion of the Board of Tax Appeals (R. 23–26) are reported in 29 B. T. A. 39. The opinion of the Circuit Court of Appeals (R. 34–41) is reported in 73 F. (2d) 5.

JURISDICTION

The judgment of the Circuit Court of Appeals, affirming the Board of Tax Appeals, was entered September 18, 1934. (R. 41–42.) A petition for rehearing was denied on October 24, 1934. (R. 42.) The petition for a writ of certiorari was filed Jan-

uary 23, 1935, and granted on February 4, 1935. The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether shares of stock held on margin are capable of identification so that a taxpayer selling part of his holdings may select, as his basis for determining gain or loss, the cost of any particular lot.

2. Whether Article 58, Regulations 74, is valid.

3. Whether, when stock is sold during the taxable year, the taxpayer may have his gain or loss computed without regard to the cost of such stock, the stock having been acquired in an earlier year.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791, 797, 815, 816, 818:

SEC. 22. GROSS INCOME.

* * * * *

(e) *Determination of gain or loss.*—In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in sections 111, 112, and 113.

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided

in section 113, and the loss shall be the excess of such basis over the amount realized.

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *.

Treasury Regulations 74:

ART. 58. *Sale of stock and rights.*—When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots cannot be determined, the stock sold shall be charged against the earliest purchases of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain. * * *

STATEMENT

The facts as found by the Board of Tax Appeals (R. 24) may be summarized as follows:

In 1928 and several prior years the taxpayer dealt in stock of the United Gas Improvement Company. He traded through two brokerage houses on margin and pyramided his purchases. Upon a

decline in the market so that his margin fell below the required percentage the brokers reduced his debit balance by sufficient sales to make up the deficiency in the margin. Upon a rise in the market the paper profits were used to increase taxpayer's holdings of the stock. By this method of operation the stock standing to the taxpayer's credit on the broker's books increased during the year from 5,300 shares to 8,000 shares, an increase of 2,700 shares. At the same time his debit cash balance on the broker's books increased from $501,865.59 to $932,822.67, an increase of $430,957.08. These changes were the results of sales by the brokers at various dates throughout the year of a total of 7,900 shares and the purchase of 10,600 shares for the taxpayer's account. Purchases and sales affecting the taxpayer's accounts were entirely through the medium of street certificates handled by the brokers, who debited and credited the taxpayer's account to reflect the transactions. At no time during the year did the brokers, on the one hand, or the taxpayer, on the other, deliver to each other actual stock certificates. The substance of the taxpayer's testimony was that each sale was made in order to increase his margin and in each case where a sale was made it was his intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount.

In determining the deficiency in question the Commissioner applied to the taxpayer's stock

transactions the provisions of Article 58, Regulations 74; that is, he applied the various sales of stock during the year against the earliest purchases of stock. (R. 17.) The Board of Tax Appeals approved of this (R. 24–26) and the Circuit Court of Appeals affirmed (R. 34–41).

ARGUMENT

In 1928 the taxpayer traded in United Gas Improvement Company stock through two brokerage houses on margin and pyramided his purchases. At the beginning of the year he had 5,300 shares and during the year he purchased altogether 10,600 additional shares and sold 7,900 shares. In computing his gain the Commissioner held that the marginal sales were not identifiable. He accordingly applied Article 58, Regulations 74, *supra,* and matched the sales against the earlier purchases.

1. The taxpayer intended to sell the last shares acquired by him and contends that this intention was identification of the stock sold sufficient to take the case out of the rule prescribed by the regulation. The case in this respect is practically identical with the case of *Helvering* v. *James L. Rankin, Executor of the Estate of Richard B. Turner, deceased,* now pending before this Court, No. 582, present term. For the reasons set forth in the Government's brief in that case, a copy of which has been served on counsel for the taxpayer in this case, we submit that a mere intent to sell the last stock acquired was not an identification of the stock sold.

In fact, there is less evidence respecting identification in this case than there was in the *Rankin* case. In both cases the taxpayer traded on margin, making identification impossible, and in both cases the taxpayer intended to sell his last acquired stock, but in the *Rankin* case the taxpayer communicated his intention to his broker, whereas in this case no such communication was made. The court below gave effect to this difference, holding in the *Rankin* case that such communication amounted to identification, but holding in this case that the uncommunicated intention did not constitute identification. As pointed out in our brief in the *Rankin* case, since the broker cannot identify the stock sold, it is not apparent how the communication of the taxpayer's intention to the broker can add anything to the intention itself. But should this Court hold in the *Rankin* case that the communicated intention was sufficient identification, we respectfully submit that the mere subjective intent in this case, not communicated to anyone at the time, and not evidenced by any memoranda or book entries of any kind, is not sufficient. To permit the bare intent of the taxpayer to control would make every case of this kind depend entirely upon the undisclosed mental attitude of the taxpayer whether formed at the time of the sale or later, and on whether the taxpayer could convince the court that he had such intent. This would encourage litigation in which the taxpayer would always have the advantage. As pointed out by the court below, the distinction be-

tween the *Rankin* case and this is that in the *Rankin* case the taxpayer tried to give effect to his intent, though, as we view it, the attempt was futile, whereas in this case, the taxpayer did nothing whatever to give life to his intent. For the reasons given by the court below, we submit there was no identification in this case, even though it should be held that there was identification in the *Rankin* case.

2. The taxpayer in this case makes the same argument as does the taxpayer in the *Rankin* case, that if the regulation is held applicable it deprives him of due process of law in that it establishes an irrebuttable presumption and is therefore void under the rule in *Heiner* v. *Donnan*, 285 U. S. 312. (Pet. 21.) As pointed out in our brief in the *Rankin* case, we think the regulation entirely reasonable as applied to marginal transactions where identification is impossible. For the reasons stated in the *Rankin* brief we submit the rule is valid.

Should this Court follow the distinction made by the court below and hold that a communicated intention, as in the *Rankin* case, amounts to identification, but that an uncommunicated intent, as here, does not, then all questions raised by the taxpayer with respect to the validity of the regulation are removed. If such should be the holding, taxpayers in every case could rebut the presumption set up by the regulation by merely following the procedure adopted by the taxpayer in the *Rankin* case. Considered in this aspect the regulation is clearly re-

buttable and *Heiner* v. *Donnan, supra,* can not possibly apply.

3. The taxpayer in this case contends that his stock market operations constituted a trade or business, and that in determining his gain or loss only the "transactions" of the current year are to be considered, without regard to "transactions" of prior years. (Pet. 2, 16–19.) As we understand his argument, it is that sales made during the tax year are to be charged only against purchases of that year. At the beginning of the tax year the taxpayer's account was long 5,300 shares. During the year he bought 10,600 shares and sold 7,900 shares and his position appears to be that the 7,900 shares sold are to be charged against the 10,600 shares purchased during the year, since only "transactions" of the current year are to be considered. As stated by the court below, there is nothing substantial in this defense. (R. 37.)

Sections 111 (a), 112 (a) and 113 (a) of the Revenue Act of 1928, *supra,* prescribe how gain or loss from the sale of property is to be computed, namely, by comparing the selling price of the property with its cost, no matter whether the property was acquired in the year of sale or in an earlier year. Until the shares, whenever purchased, are sold there is neither gain nor loss. A gain springs from the sale and the tax is imposed on the gain in the year of sale to the full extent of the gain, even though the gain is attributable to appreciation in value of the property since its acquisition in an

earlier year. Cf. *MacLaughlin* v. *Alliance Ins. Co.*, 286 U. S. 244. The extent of the gain in this case depends on the cost of what was sold, which in turn depends upon what shares were sold, the last purchased, or the first purchased, or shares intermediate the two. The burden is on the taxpayer to show the cost of what was sold. Identification being impossible, the regulation is applicable.

The taxpayer's position ignores the question of how the subsequent gain or loss from the sale of the 8,000 shares held at the end of the taxable year is to be treated, nor does he suggest how the gain in 1928 would be treated in the event he had sold more shares during the year than he purchased, i. e., in the event he had sold part of the 5,300 shares held at the beginning of the year. This serves to demonstrate the unsoundness of his position.

CONCLUSION

The decision of the Circuit Court of Appeals should be affirmed.

Respectfully submitted.

J. CRAWFORD BIGGS,
Solicitor General.
FRANK J. WIDEMAN,
Assistant Attorney General.
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Special Assistants to the Attorney General.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. 663.

JOHN A. SNYDER, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT APPEALS FOR THE THIRD CIRCUIT.

PETITION FOR REHEARING OR, IN THE ALTERNATIVE, TO MODIFY THE JUDGMENT.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court:

John A. Snyder, the petitioner, by his counsel, respectfully shows to the Court as follows:

INTRODUCTORY.

1. This case and No. 582, *Helvering* v. *Rankin*, involve the same question. They were argued March 14th-15th, 1935, and decided April 29th, 1935. The question involved in each case is as to what evidence is required to identify shares of stock sold by a broker from a margin account, so as to overcome the prima facie presumption of fact established by Article 58 of Regulations 74 (Act of 1928), known as the rule of "first in first out."

2. In the *Rankin* case this Court has held that the communication to the broker of the taxpayer's intention to sell the last acquired shares first is sufficient. On this point the opinion reads:

> "*Third.* If the facts found by the Board of Tax Appeals had been what the Court of Appeals assumed them to be, there would have been such an identification of shares sold with shares purchased as to preclude the Commissioner from applying the "First in, first out" rule."

This Court, however, held that the facts so assumed may or may not have been supported by the record and, as counsel read the opinion, the case is to be remanded to the Board of Tax Appeals for further hearing and findings under *Helvering* v. *Taylor*, 293 U. S. 507, and authorities cited in Note 6.

3. In the instant case the judgment of the Court of Appeals was affirmed on the ground that the conceded fact of petitioner's intention was not sufficient identification in the absence of proof that this intention was communicated to the broker, and on the further ground that it was not found as a fact or proved that petitioner's extensive operations on the exchange constituted a trade or business.

WITH REGARD TO THE REQUESTED REHEARING BY THIS COURT.

4. It is respectfully submitted that in so ruling this Court may have overlooked the following facts alleged in the petition on the appeal to the Board of Tax Appeals and admitted:

> (Par. VIII, R. 6) From time to time during the year 1928 the petitioner instructed said firm* to *sell for his account certain shares of said stock.*
>
> (Par. XX, R. 14.) "Attached hereto as a part of this petition and marked Exhibits B and C are summary statements by months of all the transactions in U. G. I. stock herein referred to in the year 1928 in the two margin accounts * * * showing the number of shares bought and sold * * *."

These allegations are admitted (R. 22, pars. VIII and XX. They, therefore, do not require findings in their support. Moreover the Board of Tax Appeals stated in their opinion, embodying their findings (R. 23):

> "The facts upon which the case was submitted are those alleged in the amended petition and admitted in the respondent's answer thereto and those which it was stipulated the petitioner would testify to if present. For the purposes of this report the pertinent facts may be briefly summarized."

In other words the Board found all the admitted and undisputed facts and in their opinion merely summarized such of them as seemed to the Board pertinent.

On the question of sufficient identification the opinion of the Board reads (R. 25):

> "The applicability and validity of * * * the rule of 'first in first out' are the only questions presented for decision. The same petitioner was before us in a proceeding reported at 20 B. T. A. 778, contesting a

*The respective brokers, MacDonald & Co., par. VIII, R. 6; Clothier Jones & Co., par. VII, R. 5.

deficiency arising out of similar transactions in the same stock in the year 1925. In that case we sustained the * * * rule * * * and * * * our decision was affirmed * * * 54 Fed. (2d) 57. In the opinion of the Board it was said that there was no evidence of *'petitioner's intention to sell any designated stock.'* Evidently to meet this situation petitioner's testimony was given in this case to the effect that in each sale he intended to sell the most recently acquired stock. This, however, does not establish that the sales were made in that order and *we are unable so to find* in view of the stipulated facts that there *were no deliveries* of stock *certificates*, and the transactions were entirely through the medium of street certificates *which were not identified or in any way earmarked* for petitioner's account. Consequently the facts upon which we have to go here are in no way different (save as to amounts) from those in the previous case."

5. It is respectfully submitted that in holding that

> *"The only attempt at identification found by the Board* was the uncontradicted testimony of Snyder to the effect that 'in each case where a sale was made it was his intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount in order to increase his margin and acquire additional shares of the stock,"

this Court has overlooked the above quoted excerpt from the opinion by which all the admitted and uncontested facts alleged and proved are adopted as the findings of fact.

6. This being so, it is submitted that in holding that the evidence of intention was insufficient identification, this Court may have overlooked the settled rule that where the party litigant, upon whom the burden of proof is cast by a *prima facie* presumption of fact (established by statute or regulation), offers evidence to the contrary, "the inference (of fact) is at an end." *Mobile etc. R. R.* v. *Turnipseed*, 219 U. S. 35 (petitioner's brief p. 25, reply brief p. 17, Wigmore on Evidence, reply brief, p. 18).

If the inference was at an end, then petitioner was entitled to the benefit of the inference of fact to be drawn from the alleged and admitted fact that he ordered the brokers "to sell certain shares" (*supra*, p. 3) and the undisputed and proved facts (R. 32, par. XIII), that

> "In each of such instances petitioner ordered said brokers to sell the various amounts of such stock mentioned in said Exhibits B and C * * *."
>
> "With respect to each of the items of sale of shares of stock specified in Exhibits B and C it was petitioner's intention to sell the last acquired stock first * * *."

From these established facts and from the nature of the transactions the inference of fact necessarily arises that when petitioner ordered the brokers to sell certain shares, he ordered them to sell the shares last acquired, thus bringing the instant case within the rule as to identification announced in the *Rankin* case (*supra* p. 2).

Upon this point attention is invited to the second paragraph of the portion of the opinion in the *Rankin* case designated *"Second"*, in which this Court, after rejecting the Government's contention that with respect to marginal transactions, the presumption is conclusive, says:

> "It is at most the burden of proof that is affected. For the margin trader, while being required to establish the identity of the shares in order to avoid the 'First in, first out' rule is *left free to introduce any relevant evidence.*"

It is submitted that this excerpt in substance is a reiteration of the principle stated in *Mobile etc. R. R.* v. *Turnipseed* and Wigmore on Evidence, *supra*, that when any relevant evidence is introduced the inference of fact is at an end. It can scarcely be contended that the intention of the petitioner and that his instructions to his brokers to sell certain shares at the dates and in the amounts set forth are not relevant evidence tending to establish identification.

Upon these grounds a rehearing is respectfully prayed.

WITH REGARD TO THE ALTERNATIVE RELIEF PRAYED FOR, OF A REHEARING BEFORE THE BOARD OF TAX APPEALS.

7. Petitioner, in view of the affirmance by this Court of the affirmance by the Court of Appeals of the decision of the Board, is in the position, because of "procedural entanglements*" of being unable, unless expressly authorized by this Court, to adduce available evidence to show that (a) petitioner communicated to the brokers his intention to sell the last acquired shares first (b) the brokers understood that petitioner was trading in and out on a rising market in order that he might eventually sell (as he did in the following year, 1929) a sufficient amount of the shares held on margin to pay off his debit balance and enable him to hold as a permanent investment the shares originally bought, (c) the transactions on the stock exchange were petitioner's only business transactions (except for a few weeks in January-February) in the tax year, and constituted a trade or business.

The facts which petitioner has available evidence to prove with respect to the year 1928 are as follows:

Petitioner began his trading operations in 1924 with an investment of $15,000.00 in cash. He had great confidence in the future value of shares of United Gas & Improvement Company and intended by trading on margin over a period of years on a rising market to realize a sufficient "paper profit" to enable him to acquire a large block of shares as a permanent investment. The operations in 1924 and 1925 were in moderate amounts and resulted in comparatively small profits. (*Snyder* v. *Commissioner*, 54 Fed. (2d) 57.) In 1926-1927 losses were sustained.** In 1928 petitioner was seventy-six years of age and had been in the employ of the Mechanics Insurance Company of Philadelphia for thirty-seven years, attaining the position of secretary at

*Atlantic Coast Line R. R. Co. v. Florida, No. 344, April 29, 1935.

**Net loss for 1926; $59,206.99 (Commr's statement R. 16-17).

a salary of $5,500.00. Because of ill health he took a vacation in February-March and on his return in April he attempted to resume his duties, had a heart attack, which incapacitated him from further work in the company, and thereafter for the rest of the year 1928 he gave no part of his time to the business of the company. The company, however, in recognition of his long service, has ever since kept him on in the honorary position of secretary and in 1928 and 1929 paid him the full salary of $5,500.00 a year. Petitioner paid clerks in the secretary's office an extra compensation for doing the work of the secretary.

From April on till the end of the year petitioner gave all of his time that he gave to any business matters, to his trading operations and, except for the summer months, kept in daily touch with his brokers and was in constant conferences with them as to his future operations. He made it clear to them that it was his intention to trade in and out, increase his holdings, to sell the shares last acquired, and eventually to hold the shares first bought as a permanent investment, in 1928 selling the shares from time to time, the purchase of which had impaired his account, as was the usual custom of the trade. To this end he kept in force with each of his brokers standing buying and selling orders so as to enable him on a rise to acquire additional shares and on a fall to sell enough of the last acquired shares to preserve his margin.

8. This evidence was not presented to the Board of Tax Appeals at the hearing, May 22d, 1933, for the following reasons:

(a) It would not have affected their ruling because of the decision of the Third Circuit of Appeals in the petitioner's 1925 case (*Snyder* v. *Commissioner*, 54 Fed. (2d) 57). Any review sought by the petitioner of an adverse decision of the Board must be had in that Court. In the opinion of the Court of Appeals in the 1925 case, affirming the ruling of the Board (20 B. T. A. 778) there is nothing to indicate that the communication to the brokers of petitioner's in-

tention would have been a sufficient identification to take the case out of the rule. On the contrary, the opinion of the Board of Tax Appeals in the 1925 case (as in the instant case (R. 25)), and the opinion of the Court of Appeals in the 1925 case all indicated that in order to take the case out of the rule the *certificates sold must be identified*. On this point the opinion of the Court of Appeals (54 Fed. (2d) 59) reads:

> "The broker thought, as he testified, he was selling the shares of the last purchases, though *in no way earmarked or allocated*. In other words, he *conceived* 'from the technique of Mr. Snyder's operations'—overloading the account—he was in each instance selling the shares latest purchased because it was those shares that, on a falling market, had embarrassed the account. Stated differently: But for the last purchases the account would not be embarrassed, therefore the broker sold *what he thought were the offending shares*, although a sale of shares purchased earlier would have restored the account just the same. * * * As *this was all the evidence of identification* in the case, it left the regulation, 'First in, first out,' in force and justified the determination of a deficiency tax."

Consequently it seemed necessary for petitioner, upon the hearing of the instant case before the Board, to adopt a theory which would distinguish the 1925 case, so that neither the rule of *stare decisis*, nor of *res adjudicata* might prevail.*

The instant case was argued before the Court of Appeals on the same day as the *Rankin* case. Both cases were elaborately briefed and argued. They were decided on the same day (73 F. 2, 5, 9).

True that that Court in the 1925 case had said that "something else" was needed beyond proof of petitioner's intention and of the knowledge, or assumption by the broker that the last acquired shares were the first sold

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*Before the Court of Appeals the Commissioner contended that the 1925 decision was *res adjudicata*. This contention was overruled (R. 35).

(R. 40). It was not until that Court rendered its decision in the *Rankin* case (73 F. 2d 9) that it was held by any court that *communication of the intention to the broker was sufficient identification.* Indeed it is submitted that the opinion of the Court of Appeals in the *Rankin* case on this point (now confirmed by the opinion of this Court in that case), is wholly inconsistent with the opinion of that Court in petitioner's 1925 case.

(b) At the time of the hearing before the Board in the instant case (May, 1933) petitioner was upwards of 81 years of age. At that time he was in a hospital, undergoing an operation and his doctors would not permit him either then or in the near future to undergo the strain of taking the stand or even of going into a detailed statement of all the facts. The best that counsel could do under the circumstances was to prepare a statement which petitioner approved, and have it introduced in lieu of evidence under a stipulation. The Government counsel were unwilling to stipulate further and counsel for petitioner was not informed until after the decision of the Court of Appeals in the instant case (September, 1933, by which time petitioner had recovered his health) as to the fact that from April to the end of the year 1928 petitioner's sole business activity was limited to his extensive trading operations. The schedules (R. 18-21) show that except for sales of 800 shares in February, petitioner's operations prior to May 1st were confined to purchases of 1000 shares in the Jones and 1100 shares in the MacDonald account. During the period from April 30th to December 31st he sold on various dates 3300 shares in the Jones account and 3800 shares in the MacDonald account, making with the 800 sold in February the total sales for the year 7900 shares as found (R. 24). During this same period April 30-December 31st he bought at various dates 3900 shares in the Jones account and 4600 in the MacDonald account making a total of purchases for the year of 10600* shares as found (R. 24).

*Including the 2100 shares bought prior to May 1st.

In view of petitioners great age and his serious illness with little prospect of immediate recovery, his counsel was put in the position of being forced to do as he did and it is submitted that in this very unusual situation petitioner is entitled to appeal to this Court to right a great wrong otherwise inevitable, namely a tax of $38,970.79 with over 36 per cent interest, in the aggregate over $52,000, instead of the tax of about $1,897.77* and interest in the aggregate about $2,600, a tax some twenty times as much as is justifiable.

In the opinion in the instant case, sections "*Second*" and "*Third,*" this Court has intimated that had it been found as a fact (or admitted) that petitioner in the tax year had been engaged in a "trade or business" within Section 22(a) of the Revenue Act of 1928, petitioner's contention that the transactions for that year should have been segregated and the tax computed accordingly, without reference to purchases in prior years, would have been sustained.

As appears from the above statement there is now available newly discovered evidence, which was not known to counsel until after the decision of the Court of Appeals, proving clearly under the cases cited on the point by this Court and under *Walter Thiele,* 32 B. T. A. 134, that, except for a few weeks in the early part of the year, as petitioner gave all his time to these transactions they constituted a trade or business. This evidence was not known to counsel and could not be ascertained at the time because of petitioner's illness and great age.

It is submitted that under the peculiar circumstances herein set forth the interests of justice authorize the granting of the relief prayed.

As the Board of Tax Appeals was misled quite as much as petitioner by the decision of the Third Circuit Court of Appeals in the Snyder case for 1925 (54 F. 2d 57) and as it is not a court, the same strictness is not required with

*Petitioner's brief Appendix B. p. 300).

respect to granting new trials as in the courts of first instance.

Petitioner's counsel in the instant case was not retained until shortly before the hearing before the Board. The above evidence has become known to counsel, part after the decision of the Court of Appeals and part since the decision of this Court. It is newly discovered evidence and it is clearly sufficient to support petitioner's contentions. The names of the witnesses, in addition to petitioner are Raymond H. Bailey, a member of C. Clothier Jones & Co., and Robert MacDonald, Jr., a member of MacDonald & Co.

It is further submitted that the instant case is within the spirit of the decision of this Court in *Helvering* v. *Taylor*, 293 U. S. 507 and "consonant with the great remedial purposes of the legislation creating the Board of Tax Appeals." (*Ib.* 516)

WHEREFORE, it is respectfully prayed that a rehearing be granted, or, in the alternative; that the judgment of this Court direct the Board of Tax Appeals to grant a rehearing, at which the petitioner may prove the facts above referred to, so as to identify the shares sold, under the ruling in No. 582, *Rankin*, and to prove that the transactions referred to constituted petitioner's business throughout the tax year.

JOHN A. SNYDER, *Petitioner*,
by HENRY M. WARD, *Counsel*.

District of Columbia, ss:

Henry M. Ward, being first duly sworn, deposes and says that he is counsel for the petitioner above named; that he has read the above petition; and that the same is true to the best of his knowledge.

HENRY M. WARD.

Subscribed and sworn to before me this 17th day of May, 1935.

MINERVA CLINTON,
Notary Public.

(Notarial Seal)

CERTIFICATE OF COUNSEL.

I, Henry M. Ward, Counsel for the petitioner above named, hereby certify that the above petition is in my opinion well founded, is presented in good faith and not for delay.

May 17, 1935,

HENRY M. WARD.

7.

SUPREME COURT OF THE UNITED STATES.

No. 663.—October Term, 1934.

John A. Snyder, Petitioner. *vs.* Commissioner of Internal Revenue.	On Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[April 29, 1935.]

Mr. Justice Brandeis delivered the opinion of the Court.

This case presents further questions regarding the application to marginal transactions on the stock exchange of Article 58 of Regulations No. 74, as well as some of those already considered in *Helvering* v. *Rankin*, decided this day.

Snyder was the salaried secretary of an insurance company. During 1928, as in previous years, he made on his individual account, at different dates and different prices, many purchases and sales on margin of United Gas Improvement Company stock. In his Federal Income Tax return for the calendar year 1928 he reported, apparently, no profits from trading on the stock exchange. The Commissioner of Internal Revenue concluded that he had made large gains; determined that his net income was $197,495.85; and, after making the appropriate deductions, assessed a deficiency tax of $38,961.22. The large income computed by the Commissioner was the result of applying the sales made in 1928 against purchases in earlier years, in accordance with the "First-in, first-out" regulation and §§ 111-113 of the Act. The Board of Tax Appeals (29 B. T. A. 39) and the United States Circuit Court of Appeals (73 F. (2d) 5) affirmed the Commissioner's determination. The facts found by the Board of Tax Appeals, upon which the case was submitted, are these:

Snyder traded in United Gas Improvement Company stock for profit through brokers on margin; and increased his holdings by the method known as "pyramiding". On January 1, 1928, there stood to his credit 5,300 shares; and his debit balances aggregated $501,865.59. He purchased during the tax year 10,600 shares and sold 7,900. At the close of the year, 8,000 shares stood to his credit,

and his debit balances aggregated $932,822.67. Upon rises in the market, paper profits had been used to increase his holdings. Upon declines in the market, when his margin fell below the required percentage, the brokers reduced his debit balances by sufficient sales to make up the deficiency in the margin. The purchases and sales were effected by the brokers transferring so-called "street certificates," each for 100 shares, in the name of some stock exchange concern, endorsed by it in blank. At no time was any stock certificate delivered by the brokers to Snyder, or by him to them; nor was any certificate earmarked for him or his account. The certificates were inextricably mingled with other securities pledged with banks. They were at all times incapable of identification as having been bought or sold for the account of Snyder. The transactions between him and the brokers were reflected solely in entries in Snyder's account on the brokers' books; and no entry indicated that any particular lot theretofore purchased had been sold or retained. The only attempt at identification found by the Board, was the uncontradicted testimony of Snyder to the effect that "in each case where a sale was made it was his intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount in order to increase his margin and acquire additional shares of the stock."

First. Snyder contends, in the alternative, that his intention to sell the last acquired stock first, constituted sufficient identification to make the "First-in, first-out" rule inapplicable; or else that the regulation as applied to marginal transactions on the stock exchange is invalid, because there is no possible means, other than the trader's intentions, of identifying the shares sold. What has already been said in *Helvering* v. *Rankin* is enough to dispose of both of these contentions. It is there determined that shares traded on margin are capable of identification for the purposes of the regulation; but that the mere intention of the trader to sell particular shares, without further designation, does not constitute sufficient identification.

Second. Snyder contends that the "First-in, first-out" regulation may not, consistently with the provisions of the Revenue Act of 1928, be applied to the facts of this case. The argument is that his market operations constituted a trade or business as those terms are used in Section 22 (a) of the Act; that accord-

ing to that section, and the applicable decisions of this Court, *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359; *Woolford Realty Co.* v. *Rose*, 286 U. S. 319, gross income from such business, as well as net income under Section 23 of the Act, must be computed entirely with respect to transactions within the taxable year; and that §§ 111-113, upon which the Government relies, are not applicable because they relate only to "sales of property, including securities, held for investment", and have no application to sales made in the course of a "business of trading on the stock exchange". On this assumption, Snyder argues that the income realized during the taxable year from his stock transactions is not the aggregate of the gains and losses on each sale of securities, measured by the difference between the sale and cost prices of the securities sold, but the profit or loss realized as a result of all market operations, purchases as well as sales, made during the taxable year. Such profit or loss, he now suggests, must be computed "by taking the difference between the purchase price and the sales price of shares bought and sold during the year, deducting expenses, such as commissions, taxes and interest". Thus computed, he concludes, his market operations resulted in a gross income of $43,692; and adding his salary, insurance commissions and dividends, and deducting the expenses of his stock operations (interest paid brokers) his net taxable income was $39,682, and his total tax $1,897.77.

Third. Neither in the findings of the Board of Tax Appeals, nor in the facts upon which the case was submitted to it, is there any support for the controverted allegation in Snyder's petition that his market operations constituted a "business regularly carried on for profit."[1] It is true that a taxpayer may be engaged in more than one trade or business, as those terms are used in various provisions of the Revenue Acts; and that, in addition to other business activities, one may be "regularly engaged in the business of buying and selling corporate stocks." Compare *Dalton* v. *Bowers*, 287 U. S. 404; *Burnet* v. *Clark*, 287 U. S. 410. *Washburn* v. *Comm'r of Internal Revenue*, 51 F. (2d) 949. It is also true that the Depart-

[1]The answer of the Commissioner denied that the "brokerage accounts . . . constituted a trade or business within the meaning of any provision of the Revenue Act of 1928." The Board of Tax Appeals made no specific finding on this issue; but the Court of Appeals assumed that the Board meant to find against the taxpayer, and concluded that the assumed finding was supported by the evidence.

ment has ruled, and the Board has held, that a taxpayer who, for the purpose of making a livelihood, devotes the major portion of his time to speculating on the stock exchange may treat losses thus incurred as having been sustained in the course of a trade or business.[2] Snyder, however, did not allege or attempt to prove that he had devoted the major part, or any substantial part, of his business day to his stock transactions. Nor were there any facts adduced to show that he might properly be characterized as a "trader on an exchange, who makes a living in buying and selling securities". *Bedell* v. *Comm'r of Internal Revenue*, 30 F. (2d) 622, 624; compare *Mente* v. *Eisner*, 266 Fed. 161. Indeed, according to his petition, his intention throughout the year 1928, was, by "taking advantage of the turns of the market," not to draw out cash profits from his operations, but "to increase the holdings of U. G. I. stock carried for his account by [his] brokers to as great an extent as the margin of his account permitted." There is no substantial evidence in the record to sustain a finding by the Board, had there been one, to the effect that Snyder's market operations constituted a trade or business within the meaning of Section 22 of the Revenue Act of 1928.

Fourth. The attack upon the Commissioner's method of computing income falls with the unsupported allegation that the stock transactions constituted a "business regularly carried on for profit." In his brief in support of his petition to this Court for certiorari, Snyder makes it clear, perhaps for the first time, that he is "insistent upon the point that the operations constitute a trade or business or transaction entered into for profit, not in order to deduct losses, but to emphasize the controlling rule that the law requires the tax to be computed on the segregated transactions of the year." But it is now too well settled for argument, that gains realized from sales of property purchased in previous years, measured, as prescribed by §§ 111-113 of the 1928 Act, by the excess of proceeds of sale over cost, constitute income taxable in the year in which the sales are made. *Doyle* v. *Mitchell Bros.*

[2] I. T. 1818, II-2 C. B. 39; Schwinn v. Comm'r of Internal Revenue, 9 B. T. A. 304; Elliott v. Comm'r of Internal Revenue, 15 B. T. A. 494; Hodgson v. Comm'r of Internal Revenue, 24 B. T. A. 256; Schermerhorn v. Comm'r of Internal Revenue, 26 B. T. A. 1031. Compare Black v. Bolen, 268 Fed. 427; Rogers v. United States, 41 F. (2d) 864; Kunau v. Comm'r of Internal Revenue, 27 B. T. A. 509; Thiele v. Comm'r of Internal Revenue, 32 B. T. A. —, decided Feb. 26, 1935.

Co., 247 U. S. 179, 184-5; *Hays* v. *Gauley Mountain Coal Co.*, 247 U. S. 189, 192; *MacLaughlin* v. *Alliance Insurance Co.*, 286 U. S. 244, 250. The contention that the rule is applicable only to the sale of capital assets and not to sales made in the course of a "business of trading on the stock exchange", need not be disposed of on its merits, but see *Gray* v. *Darlington*, 15 Wall. 63, 66; *Merchants' L. & T. Co.* v. *Smietanka*, 255 U. S. 509, 520, since Snyder has failed to establish that the securities sold were held primarily for sale in the regular course of business.[3] And obviously, whether or not the stock transactions constituted a trade or business, the computation of gross income therefrom by deducting from sales of the current year the cost of securities sold, as determined by the purchase prices of previous years, is not comparable to the unsuccessful attempt in *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359, to offset gross income of the current year against losses or expenses of previous years.[4]

Fifth. Moreover, Snyder suggests no other practicable method of accounting which would reflect income for the year more fairly than the method adopted by the Commissioner.[5] He concedes that he is not a dealer in securities, in the sense of one who buys securities for the purpose of resale to customers; and that consequently, he is not entitled to compute income on an inventory basis.[6] Compare *Lucas* v. *Kansas City Structural Steel Co.*, 281

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[3]Compare Hutton v. Comm'r of Internal Revenue, 39 F. (2d) 459, where the deduction of brokers' commissions on purchases of securities, as business expenses, was disallowed. The Board found that the taxpayer was "engaged in the business of buying, holding and selling realty securities, etc."; but regarded the commissions as "capital expenditures". 12 B. T. A. 265. Compare Vaughan v. Comm'r of Internal Revenue, 31 B. T. A. 548; Keeney v. Comm'r of Internal Revenue, 17 B. T. A. 560.

[4]Proceeds from sales in the regular course of business constitute gross income of the business only to the extent that they exceed the cost of the goods sold. See Spring City Foundry Co. v. Commissioner of Internal Revenue, 292 U. S. 182, 185. Compare Washington Land Co. v. Comm'r of Internal Revenue, 10 B. T. A. 503; Atlantic Coast Realty Co. v. Comm'r of Internal Revenue, 11 B. T. A. 416; Stern v. Comm'r of Internal Revenue, 14 B. T. A. 838. See Art. 55, Regulations 74, Revenue Act of 1928.

[5]Snyder does not attempt to bring himself within the general rule of section 41 of the 1928 Act, to the effect that "net income shall be computed upon the basis of the taxpayer's annual accounting period in accordance with the method of accounting regularly employed in keeping the books of said taxpayer". Neither does he state that the method he now suggests was followed in his return.

[6]Article 105 of Regulations No. 74, permit dealers in securities to make returns on inventory basis. A dealer is defined as a "merchant of securities, . . . with an established place of business, regularly engaged in the pur-

U. S. 264, 268; *United States Cartridge Co.* v. *United States*, 284 U. S. 511, 520. His suggestion that gross income from trading be computed by deducting purchase prices from sale prices during the year would offer a feasible substitute only if it could be assumed that the number of purchases and sales would be approximately equal each year and that any differences would be averaged out in the course of a number of years. That assumption is unwarranted, particularly in view of Snyder's professed object "to accumulate as many shares of U. G. I. as he could."[7] His alternative suggestion, that, since purchases in fact exceeded sales during 1928, the "First-in, first-out" rule, if applied at all, should be confined to purchases and sales in the course of the year, adds nothing to the contentions that have already been considered in this case or in *Helvering* v. *Rankin*.

Affirmed.

Mr. Justice STONE concurs in the result, but thinks that the petitioner failed to show that the particular shares sold were capable of identification with respect to the date of their purchase, and that they could not be identified merely by the taxpayer's designation of them to the broker as the shares to be sold.

A true copy.

Test:

Clerk, Supreme Court, U. S.

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chase of securities and their resale to customers." Compare Harriman National Bank v. Comm'r of Internal Revenue, 43 F. (2d) 950; Pan-American Bank & Trust Co. v. Comm'r of Internal Revenue, 5 B. T. A. 839; Adirondack Securities Corp. v. Comm'r of Internal Revenue, 23 B. T. A. 61; Northeastern Surety Corp. v. Comm'r of Internal Revenue, 29 B. T. A. 297; Lowell v. Comm'r of Internal Revenue, 30 B. T. A. 1296; Fried v. Comm'r of Internal Revenue, 31 B. T. A. 638; Brendle v. Comm'r of Internal Revenue, 31 B. T. A. 1188.

[7] In Snyder's computation, although he purports to take "the difference between the purchase price and sale price of shares bought and sold during the year", the cost of the last 1,500 shares bought in one of his two brokerage accounts during the year is deducted from the total cost of purchases in that account, because purchases exceeded sales by 1,500 shares.